

# WHAT IS THE KEY TO SUCCESSFUL SHIP MANAGEMENT

By

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## Introduction

For centuries man has been roaming the world's oceans on various forms of ships and seafaring was a daring venture nothing short of going to the moon, undertaken by men of vision with great courage and personal skills. In the early days of seafaring, ships were largely managed by their crew, notably the Master, which is still true today. Let us not forget this crucial fact in our forthcoming discussion, that the crew is always the backbone of ships operation. Any management measures will only ensure maximum performance of the crew while any management system that alienates itself with the ship hands is self-defeating.

But what had driven the need to set up a back-office ship management function to support the ship's crew? This apparent basic question is seldom revisited by our very own industry. By reflecting upon the original values that created the ship managers, it would be readily realised that the future direction of this business can simply be found in its own history.

## Evolution & Growth of ship management business and its traditional model

Ship management evolved from an in-house function of the ship owners and the tasks of operating ships had instigated the need for a formal organisation to manage their vessels, performing the most basic functions of crewing, maintenance, supply and compliance with statutory matters. It is not difficult to trace the links of many successful independent ship managers to some form of ship owning interests in their business ancestry.

Early development of independent ship management was a result of ship owners trying to overcome the constraints of the adverse fiscal regimes of national registries and prohibitive crew labour costs.

Till the early 1980's, the independent ship management business grew rapidly because many ship owners were suffering from high operating overheads in the face of a depressed freight market and outsourcing

of the vessel operations to a ship manager was seen as an effective method for reducing operation expense.

However, due to the absence of any entry barriers and minimum requirements, a proliferation of independent ship managers began to take shape. By the late 1980's, the actions of the maverick "managers" were of great concern to the independent ship managers who were operating responsibly and properly.

In 1989 the top executives of five leading independent ship management companies joined together to draft a code of practice for the industry. This code included a mechanism for independent verification to ensure quality, professionalism, and integrity in all aspects of a ship management operation and was the basis for the formation of the International Ship Managers Association (ISMA) in 1991.

With the advent of ISMA, Quality became a buzzword and vessel owners, along with others who utilised ship manager's services, began to draw a distinction between the "mavericks", who's days were now numbered, and the responsible, professional ship management companies. The industry could finally make a distinction between managers and began to acknowledge the value of ISMA certificated ship managers. Large and traditional ship owning institutions began to entrust their vessels to ship managers with the objective of not only reduction in operating costs, but also improvement in vessel turnaround and efficiency, and long-term asset preservation.

The second wave of reform came in the early 1990's when the International Maritime Organisation (IMO) began its campaign for Safer Ships and Cleaner Seas. This IMO initiative culminated in the drafting and approval of the International Safety Management Code (ISM) which came to effect on 1 July of 1998 and is fully implemented for every type of vessels in 2002. During the same period, STCW 95 that attempts to structure shore based and ship board training is also fully implemented.

## **The changing face / Structure of the Ship Management Environment**

As ships become safer and arrival a more or less certainty to be expected (in contrast to the old days when peril at sea was as much to be contemplated as a bountiful home coming from a venture into the high seas), public perception to seafaring risks changes from being accepted hazardous ventures to being regular transit passages. Any form of mishap becomes exceptions and the expectation of safety at sea is heightened as industry confronts new challenges.

### **Impact of increasing legislative requirements**

Increased emphasis on compliance with legislative requirements over the last few years has added more weight in procedures than in people in all aspects of the ship management process. There has been counter argument that the detail and definition in the revised Convention, together with the detailed manuals and procedures lead to an over-emphasis on training in the sense of a structured and deliberate learning process. In addition, there has been a diminution in job satisfaction and in the attractiveness of a seagoing career--which relates directly to the redundancy of many traditional skills, the decrease in manning levels, the return of casual employment and the unsociable nature of today's industry.

By no means of course, the introduction of any of the legislative requirements intends to cause any undesirable effect. To actualize the value of these requirements, there is a need for the management to cater for the matching tasks, such as adjusting the training focus on people development, building the right working culture, facilitating a motivational learning environment.

### **Impact of migration of manning resources**

It is an undeniable fact that ship owners have been operating in an extremely undesirable freight and ship-value market in recent years. Both ship owners and shipmanagers are operating within a squeezed budget. In order to gain competitiveness over each other, shipmanagers are working hard to reduce their overheads on one hand, and on the other, they respectively seek to develop and exploit competitive manning resources.

Countries like India, China, Indonesia and some of the East European countries are seen as highly potential

recruiting centers in the new era.

How do ship managers add value to new crewing resources in today's more open and accessible market? What is the value contribution of a crew manager when compared to a manning agent?

### **Impact of migration of skill requirements**

Have ships become more reliable and thus have the skill requirements of crew changed in respect of technological advances in ships?

As ships become safer and consistently more foolproof with ever higher level of automation and reliability, is the demand of traditional seafaring skills fading away? The values of human intervention may be changing from correctly performing a series of tasks to monitoring the same tasks and intervening only in complex situations where automatic processes cannot come up with a solution. Airline pilots are classic example of such shift of skills. Is seafaring following the same footsteps? With more advanced vessels, should the modern crew be better trained in dealing with complex hazardous situations?

### **Impact of exploitation of IT development**

Today, technology revolutionizes traditional operation processes in all business contexts. The ship management business is no exception. Does the traditional ship management business find itself into a B2B e-commerce business model through 'substitution', 'scale' and 'structural' transformation?

### **Key Business Constituencies and Respective Values as Critical Success Factors**

With the ship management process heavily regulated and monitored by various authorities, ship managers' role, in respect of their core function to ensure safe and timely transportation of cargoes from one end to the other, has not changed. What has changed is the traditional perceived value that ship management companies adds in to the ship operation process that has become marginal, however critical.

In addition to the emphasis put on quality procedures, rapid development of technologies that enable efficient information flow between ship-shore and greater extent of automated operational processes, pose further threat to the traditional model, in transporting the shipboard decision making largely to shorebased establishments.

Having said that, I don't mean at all that the future

for ship management companies is pessimistic. It really depends on how we perceive and respond to that challenge. In this respect, the challenge is essentially a matter of how efficiently we can leverage our resources, that is, our people, processes and technology in our service delivery to meet our customers' needs.

When determining or anticipating customers' needs, we must realize the fact that ship management, is an integral part of the value chain in shipping. If we have a better understanding on our customer's earning cycle, we may be in a better position to view and anticipate changes in our role, and hence, seek room to maintain or add weight in the value chain.

A "told to do" era has gone long time ago. Quality assurance is not sufficient to sustain competitiveness. Value creation is the key to success. A ship manager, like most other businesses, consists of three key business constituencies, i.e. customers, employees and shareholders. Each constituency carries its own values and all of which are fundamental to the business operation. The management of the company is tasked with this role to align these values with a balanced focus in achieving the business goals. Effective creation of the values is critical to the success of the business.

### **Customer Value**

Ship management fees have been driven down to a level that managers generally find it impossible to reduce further without affecting quality of services, yet owners are consistently demanding lower fees taking advantage of the fierce competition.

To sustain a reasonable contribution from the business, bearing in mind the shareholders interests have to be taken care of as well, requires packaging more values in the management services, values which customers are willing to pay for.

It is a fact; customers do lend us endless strength and drive us to building our own competitiveness and success. However, in the ship management business context, there is something more than just competitiveness. In our business philosophy, it is integrity and loyalty. Just the same as what we require from our seafarers, to be honest and committed to the assignment entrusted to them to ensure that jobs are well done to the extent of achieving and exceeding given safety and quality standard. In our role as a ship manager and being fully responsible for the outcome of the ship operation that our customer entrust to us, other

than achieving international safety and quality standard, the ultimate value out of the ship management service that we deliver to our customers is very much to do with total customer experience. We are all driven by customer expectation and where possible we try to surpass it with a view to build long-term customer loyalty and commitment.

At this point, some may argue that anything delivered beyond the basic requirements for safe operation of a ship is a waste that will only increase cost of operation and hence against the customers' interest. Bearing in mind that we are part of the value chain in the entire shipping process, our relationship with our customers is basically business to business, which is only part of the entire value chain. How our value (Shipmanager's value) to the customer is essentially weighed as the contribution made in increasing the customers' competitiveness down the line of their business cycle is of critical importance. Everything we do, what and how, is a cost-benefit decision, either with an immediate value, or with a value to be migrated to the next customer in the line.

### **People Value - Shore staff and Seafarers**

To succeed with customers, we must succeed with our people. The challenge lies with how to create in the organization and in its people the desire to achieve excellence, the belief that it is achievable, and the capability and motivation to see events through to success.

In a value creation process, prior to effective process and advanced technologies, we need the drive, the drive of change for the better. We require initiatives of people to seek and apply methodologies and tools to re-engineer their work process, reducing cycle time and improving service quality, and hence delivering a greater service value to the customers. A greater service value apparently increases competitiveness of the customers either in a way of direct cost saving in the ship management budget by streamlining processes, or better preservation of asset value through improved quality of maintenance, greater care and better knowledge in cargo handling etc.

Having said that, creating this commitment in each individual is still something easier said than done. The struggle is basically why we need to change and what is in it for me following that change? The answer to why such reservation exists is likely to be: either people do

not see the potential turbulence that lies ahead in their journey or they fail to see the value imparted to the individual through the change process.

Apparently, people sailing in stormy weather are more prepared to react. Those sailing in calmer seas for too long tend to become complacent. However, resources can be utilized in a more effective manner in peaceful time. The challenge to management in this respect is how to motivate people to think ahead and act pro-actively when the business is in calmer seas. So, let's think about the benefits to individuals and look for an effective motivator. An effective motivator is usually linked to the reward system. A reward system with only emphasizes on monetary incentives however may not be effective as it encourages people to focus on the short term benefit and therefore ignores the potential threat that require individuals to shape up and be prepared for a longer journey.

Apart from motivation aspect, management's role in the value creation process is largely on facilitation. Management has to plan and provide the resources necessary for building a quality culture and for enlarging the skill and knowledge database of individuals. People are the key assets of shipmanagers. Before we can turn to management for transforming our human capital into delivering a value added service for our customer's benefit, what are the values the management should deploy and add to the huge pool of human assets under their management? We will look into these facilitation approaches in a later section applying a knowledge-focused strategy.

### **Shareholder Value**

The key objective of CEOs and their teams is to maximize the return on investment for shareholders in the business. To achieve this objective, they must focus on finding unique ways to serve customers. In any business, financial performance ultimately depends on creating Capturable Customer Value (CCV) as efficiently as possible. The businesses that create most shareholder value are those that can create the highest CCV, not merely the most efficient businesses.

Creating shareholder value begins with creating benefits for customers, and figuring out how to capture the optimal capturable customer value. This is the link between customer value and shareholder value, which applies to all companies.

In addition to profit, other values that we owe to our shareholder include our business viability, brand equity, organization development and market share. As a whole, the ultimate value we add to our shareholder is in the corporate intellectual capital value, which ensures continuous competitiveness and growth of a business.

### **The Process of Effective Value Creation: Strategic Choices**

When customers select our service, it is because they perceive a value in the benefits they can derive from the services offered by us. This value depends both on the service and on the customers' needs. For instance, a specialized crew with exceptional experience and skills in a particular type of cargo could be crucial to fulfill a charter party requirement worth millions of dollars.

In reality, the customer value that we can capture and realize into revenue does not quite correspond to the absolute value of the service. As a matter of fact, it is often significantly lower, such as the management fee earned by the shipmanager as compared with the freight earned by the ship owner.

This is largely because of the competition in the market. A well-established pricing structure exists in the ship management market that is more closely related to the cost of supply than to the value of the benefits which customers can derive. This is a classic model of near perfect supply side market, i.e. almost an infinite elasticity of supply.

One way to get out of this situation can also be found in elementary Economics textbooks. Product differentiation will shift the supply curve away from the perfect competition model. The more we can differentiate our services from competitors, the more capturable customer value will be available to us.

In the conservative world of shipping, many may dispute the possible extent of service differentiation applicable to ship management business. Finding such rooms for product differentiation is exactly where innovative management proves their worth. Any ship managers' strategic approach rests with real customer values creation.

Hence, two key drivers of the capturable customer value are identified as product/service distinction and utility value of services.

To maximize value creation in the ship management process, we consider applying the following strategies to exploit this aspect to full extent.

### 1) Customer Relationship Management (CRM) Strategies

It is often said that the cost of acquiring business from a new customer is at least 5 times more than from an existing client. This is so true for the ship management business. Before a ship owner will entrust assets worth tens of million of US Dollars to a shipmanager's care, it is not difficult to imagine the lengthy process that both have to go through from the point of getting to know each other, to assessing the management process capability, to ascertaining one's competitiveness. The cost of a shipmanager investing in a new customer before they can successfully sign a service contract is far beyond the norm.

Customer relationship management is a strategy that is geared to achieving customer loyalty and is significant to the cost effectiveness of the ship management business. During the process of cultivating customer loyalty, customer strategy, people and business results are linked. Therefore, the core action of the strategy is about building organizational capability to address strategic imperatives and to produce desired business results.

The key for companies to achieve customer retention is customer information. The more we know about our customers, the better we can tailor our proposition to them and the more likely they are to stay with us. But while we are making attempts to hear from our customers whether in the form of survey or personal contact, we have to make sure that we put in equal amount or more efforts to learn from the customers' feedback and ready to do things differently as a result.

Simply satisfying customer's need is not sufficient to earn loyalty. A merely satisfied customer will go elsewhere when the competition cuts its price. Customer buys for a variety of reasons, but the main reason customers leave is poor service. What we need to offer is a customer experience that provides value. For example, it is shipmanager's basic responsibility to submit vessel variance report to their principal on regular basis. We can choose to meet this basic requirement as per customer's request or

alternatively, we can seek to establish infrastructure to enable customers to access the necessary information any time at their own pace. Real time information adds a value to the customer allowing them to plan ahead and act on time when necessary. If we would treat every customer like our sole customer, we would never have to worry about repeat business.

### 2) Knowledge Management (KM) Strategies

People are the fundamental resource in the ship management process. The skill, knowledge and experience that every individual whether working on board or in the shore office carries, constitutes the human capital of a ship management company.

Knowledge management is an effective strategy enabling value creation through a structured process of knowledge sharing. The KM model consists of three components i.e. human capital, structural capital and customer capital. Optimal leverage of these components increases the intellectual capital value of an organization.

In the ship management business context, this strategy can be applied to create value effectively by maximizing the knowledge flow across the global operational network covering knowledge input from shore and ship staff.

In the implementation process of KM, company management sets strategy and enables the set up of necessary infrastructure to support knowledge flow and to create a knowledge sharing culture and a learning environment in the work place.

The scope of knowledge can be very broad--varying from operational experience, incidents report analysis, technical skills and knowledge to customer information. A structured process is necessary to regulate the knowledge flow and validate inputs to the system.

Effective application results in the innovation of products and services, development of new work practices and processes, to achieve higher quality and safety standards, loss prevention, individual and business growth etc.

### 3) Re-Aligning and Enhancing Core Values

No business can sustain any growth if the core functions are neglected. It makes good sense to

revisit these values at times of stern competition and stagnant growth to look for breakthroughs. After all, it was these core functions that started off the business and they represent the highest value to the customers.

Re-examining the ship management functions, we can identify the followings:

The need for expertise in technical operation of ships:

Management offices have long been playing a largely supervisory role, in terms of monitoring and control of the sea staff performance. Current emphasis on formal quality management system and the introduction of ISM demands more stringently organised approach to perform such functions. But unified standards while serve well in lifting over all quality in the industry; they have diminished the differentiation of individual managers. To recreate qualifiable values in the technical management spectrum, one possible way is to break away from the reactive approach of supervisory to a proactive approach of advisory by the shore management office. The advisory role is not only applicable to the sea staff but also a viable value creator to the customers. More specifically, the traditional practice of status reporting while necessary, are not sufficient in values, at least not sufficient for a manager to become outstanding.

Following this argument, ship condition reporting shall have to be enhanced with recommendations for improvement; budgetary control shall have to be augmented with cost saving measures. Maintenance works carried out and records filed by crew with the office shall have to be met with guidelines and periodic update of more efficient and effective practices.

Distinctions can be regained by capitalising specialisation of ship types. Ship owners can readily appreciate the benefits of using professional services with specialised experience. By specialisation it dose not mean that ship managers shall limit their scope of services to particular type of vessels but rather to develop distinctive practices, organisation and staff, including specialised crew, to manage specific types of ships. The distinction must be made visible and tangible to the customers.

Ship managers shall have to take up more initiatives in research and development of ship operations. The industry has been largely looking to classification societies and academic institutes for such support, and

the ship managers have plenty of room for generating extra values by creating knowledge from their first hand experience with ship operation.

The need for qualified people:

Supply of crew is the primary function of the ship manager and one of the most competitive aspects of the business. The basic exercise of recruitment, screening seafarers for proper qualifications, valid certificates and organising roster plans can no longer justify the values of a manager. Such kind of services can be readily available from manning agents, who are most willing to capture this market at a fraction of the cost charged by the ship managers. Additional value is derived from supplying a coherent crew instead of supplying individuals, the ship manager shall have to build proven teams to realise its own value.

Another traditional value of crew management is the ability to assemble crews of different nationalities, to exploit the benefits of cost differentials between different countries while maintaining a uniform standard of performance. The manager must be able to stay ahead of the norm with a vision so as to be able to identify and develop alternative human resources before the general needs are felt. But not everyone can be the leader. For the late starters, at least the ability to bridge the cultural gaps with new manning resources is the basic value ship owners are looking for from their crew managers. However, implementation of STCW-95 further shifted the values towards the training institutes and manning agents since the standards of seafarers are perceived to be common once they acquired the STCW certificates. The ship managers, in order to retain their distinctive competence, must not only be able to perform the task of team building and handling the intricacy of multinational crew, but be able to demonstrate such abilities convincingly to their customers to prevent erosion of their identities.

Regulatory Functions:

We have already covered the impact of rules and regulations on ship management industry, commencing from self-regulatory stage with the voluntary membership of ISMA and ISO 9000 or other formal Quality Management System, to the advent of mandatory ISM.

But experience shows that such paper chase is not going to enhance the true value of ship management service. The illusion of creating barriers to entry for new

competitors as well as making it more difficult for ship owners to operate their vessels with more regulations has been proven counter productive. On one hand the international community is sufficiently flexible to allow ample time and latitude to ensure almost everybody can comply with new standards, to such an extent that even the function of weeding out the less stringent operators becomes questionable, on the other hand, the costs of implementing restrictive exclusion measures as such may not be justified with increased business and revenue. Regulations and formal quality control programmes exist for their specific regulatory purposes and should be respected by the players in the industry. Compliance with them cannot be relied upon as competitive tools, and customers usually see it as a duty and not an added value of their managers.

Having said that, additional value can be derived from this context in a manner recognised by the customers, this is when the manager can go one step forward and contemplate changes in regulatory control, thereby advising their customers of the impact and necessary business preparedness to absorb them. The ability to do this will be perceived by customers as valuable contributions forging a strong customer relationship.

The commercial convenience:

Independent ship managers have served the function of disassociating of the ownership from operational responsibility hence liabilities. This value is seen to be diminishing with current initiatives from the international community. The Exxon Valdez disaster had highlighted the issue of collective liability with the OPA-90 exposing owner and manager alike to face the consequences. The more recent Erika disaster has heightened this problem and the European community has reacted and already some ship owners are withdrawing their tankers from managers. Since if the risk is not transferred they are better contained! But there are owners still willing to entrust their tankers to the managers, for recognition of their superior expertise. This only proves that such aspects -as "doing the dirty work" cannot stand up to the tests of time and wisdom, but only true core competence does.

There is yet another commercial function in overcoming geopolitical barriers in trades, financing, taxation etc. in using independent managers to operate ships on the owners' behalf. This value will persist for

as long as differences exist across national borders. The ship managers will continue to derive values for their customers by bridging imposed restrictions to a perfect free market.

Economy of scale:

Any investor interested in shipping ventures will have to establish a complete and accredited management structure to operate the ships, or on the other hand, a professional manager can take up the gap to this barrier of entry.

Small owners find it cheaper to let managers operate their ships due to economy of scale. Even large owners may reach the point of diminishing return from their own management staff and go for independent managers.

To realise this value, ship managers must be able to build up their organisation to handle their target fleet size, that is, to build in economy of scale to capture the market surplus. Therefore the manager value in this respect is in quantum instead of progressive. The manager must invest in capacity to impart economy of scale or else only the largest managers will survive. To execute this strategy effectively, the manager must be able to create marginal capacity at a lower marginal cost compared to their customers. One way of achieving this is by adaptability, and mobility, again to capitalise on relative cost differential of different countries with ability to do so more effectively than their customers. It takes great resolve to commit investments and to break new grounds, this is where the value lies.

Under the concept of creating available capacity, the professional ship managers will continue to facilitate owners with flexibility in managing extreme fluctuation in their business cycles, and ease of entry into ship owning business by providing charter cover without having to develop operational infrastructure.

## Conclusion

The key factors attributing success in ship management business rest with value creation.

New values are difficult to come by in a traditional industry but old and proven values can be extended, modified and more importantly adjusted to adapt to ever-changing business environment. To work with one set of values held sacred and preventing critical re-engineering of the value chain is a major stumbling block to not just ship management but all businesses alike.

Complacency is the hurdle to higher achievements, particularly when there is actually nothing worth being complacent about, like old empires embracing lost glory and failing to grasp the new values in a relentlessly evolving world order, they are destined to rot away.

But value creation must centre on core competence, yielding true values addressing to the customers' core

interests and better still, projecting the customers' interest. There is the tendency of creating false values in the process of searching for market breakthrough. This is like what is commonly known as face-lifts in the motor industry. They are invariably short-lived stopgap measures. No face-lifted model had and ever will become a classic.

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*Since 1980 Mr. Bajpae has held senior management positions in ship management companies in Hong Kong. He is currently President and Group Managing Director of the Eurasia Group of Companies, which is a member of the Hamburg based Schulte Group. Today, the Eurasia Group includes three regional operating units respectively Eurasia International (China) Limited Partnership in Hong Kong which also has its representative office located in Shanghai, Eurasia Maritime Management (India) Pvt Ltd. in Mumbai and Eurasia International (Singapore) Pte Ltd in Singapore. Each renders a wide range of ship management and maritime services. All ship management units are supported by a training and recruitment unit of the Group, Paramount Shipping & Management Pvt Ltd that has offices in Mumbai and Delhi.*

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