THE 2001 CAPE TOWN CONVENTION
ON INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT

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The Luxembourg Rail Protocol
Enhancing the scope of Financial Services Centres (FSCs)

To maintain healthy growth in the current regulatory environment, FSCs need to be creative and find fresh business opportunities. A new international legal framework, the Luxembourg Rail Protocol to the Cape Town Convention, offers substantial advantages for investors – and exciting prospects for FSCs. Ratifying the Protocol improves the attractiveness of a contracting state for private sector financiers having their principal place of business there, as it makes raising secured credit both cheaper and easier.

Railway expansion is steady – but held back by a vast funding gap
The railway sector is experiencing steady growth, with worldwide annual spending on new rolling stock now approaching **EUR 60 billion**. Today, this is mainly financed or underwritten by governments. The result, however, is budgetary constraints to railway growth at a time when more investment is urgently needed to improve environmental sustainability, connect neighbouring economies and encourage inclusive economic growth.

Private finance of rolling stock is a key part of the solution. According to calculations using figures from the McKinsey Global Institute, there is a **global rail investment gap of USD 80 billion.** So the potential is enormous. This is where the Luxembourg Rail Protocol comes in.

A new international treaty offers the solution
The Rail Protocol is a protocol to the Cape Town Convention, a global treaty providing for the recognition and prioritisation of security interests held by private sector creditors lending on, or leasing, high-value mobile assets. As such, it addresses the key obstacle to widespread and affordable private sector funding of rolling stock: risk.

Covering a wide range of equipment – that is now trackable
The Rail Protocol will apply to leases and security created on a broad range of rail equipment, from high-speed trains, to metro trains, trams, freight locomotives, airport shuttles and harbour gantries on tracks. It will establish a new international registry for security interests operating in a secure cloud, with the registrar located in Luxembourg. The registry will be searchable online 24/7. It will also establish a unique global numbering system (a first for the rail sector) that will make tracking, maintaining, insuring and monetizing these valuable assets very much easier - even across borders.

Attractions for financiers

When financiers provide credit secured by the financed equipment to a customer domiciled in a state that has adopted the Rail Protocol, their creditor rights will be recognised and enforceable internationally, and registrable at the international registry, establishing the priority of these rights over subsequently registered claims. The registry will also allow third parties, e.g. other financiers or purchasers, to search for claims on the asset concerned, which will not only improve enforcement but also help to combat fraud and transactional mistakes.

Banks and leasing companies finance themselves via debt and equity. When an FSC state has adopted the Rail Protocol, financiers located there will be able to lay off debt through third-party institutional or bank finance, syndicated financings, or securitisations, with the interest of the holder of the collateral, the railway rolling stock, protected under the Rail Protocol.

Demand set to expand

Because investors financing companies and structures domiciled where the Rail Protocol is in force benefit from this secure new international system, they will be much more willing to lend at affordable rates, even to operators in countries they may previously have avoided.

Drawing on the very positive experience of the Aircraft Protocol to the Cape Town Convention, in force since 2006, the Rail Protocol will significantly increase the volume of private funding available and the size of the rail equipment industry, while reducing costs for operators, facilitating operating leases, and driving up demand:

- More credit will be available, leading to a more competitive lending environment.
- Lower risks mean banks have lower capital allocation requirements, leading to lower margins for borrowers.
- Lower risks also mean lower rewards required by creditors, so reduced costs for borrowers.
- Thanks to lower risks, there will be lower export credit agency financing costs.
- Documentation will be easier to produce, reducing transaction costs.

Ireland ratified the Aircraft Protocol in 2006 as part of its strategy as one of the world's leading financial services centres. Today it has:

- **50+** aircraft leasing companies, supporting
- **5000** jobs, adding
- **EUR 550m+** to the local economy.
- **60%+** of the world's leased aircraft are managed from Ireland.

The Rail Protocol offers growth to FSCs – even without a domestic rail network

FSCs in states that have ratified the Rail Protocol will have a compelling advantage to offer financial institutions lending on or leasing railway equipment. Since what counts is the debtor's legal domicile, not where the rolling stock is located, a small island nation can become a leading centre for railway finance. So ratification of the Luxembourg Rail Protocol offers excellent growth prospects to FSCs. The earlier this happens, the greater the potential to gain a competitive edge and major market share of the growing railway equipment sector.

For more on the Luxembourg Rail Protocol, visit www.railworkinggroup.org. Keep up to date with all the latest developments via the Rail Working Group's LinkedIn group page.