Putting trains back on track

The Luxembourg Protocol makes financing rolling stock easier and less risky.

Howard Rosen calls for African governments to ratify it to keep railways on the move.

A new railway line without rolling stock is like a new car without petrol. It looks impressive but it will not get you anywhere anytime soon. The problem is, it can be much easier to raise financing for a fixed railway line than movable rolling stock.

It was ever thus. In the 19th century, British railway builders created an excellent rail infrastructure, and then waited in vain for operators to provide the trains. In the end, the owners of the infrastructure had to raise the money themselves to finance the rolling stock.

This is partly because big infrastructure projects capture the imagination and focus of governments and donors, and it is easy to forget the true objective of the exercise is to provide rail transport, not simply to build railways.

Second, in Africa, it is difficult for lenders to take security interests in rolling stock that can successfully traverse the continent and all its different legal systems. Why lend money against an asset where your security can be compromised at any moment?

Securing mobile assets

Fortunately a new form of help is at hand and its source is African. In 2001, 58 countries met in Cape Town and, under the auspices of the International Institute for the Unification of Private Law (Unidroit) and with the sponsorship of the South African government, adopted the Cape Town government on International Interests in Mobile Equipment. This created a legal framework for financing high-value movable equipment with greater levels of security through private sector capital.

A protocol applying the Convention to the aviation industry was adopted in 2001 and is now in operation in more than 20 countries across the world, including parts of Africa. In February 2007, 42 governments met again in Luxembourg and adopted a protocol to the Convention extending the legal regime to all types of railway rolling stock, from trams to TGVs, and from locomotives to flatbed wagons.

The Luxembourg Rail Protocol creates an international private law system for recognising priorities of secured parties, usually banks or lessors, financing rolling stock. Registering their security interest at an international registry available 24/7 through the internet, ensures they have priority against other subsequent claimants as a matter of law.

At the same time this creates a system for prospective financiers of rolling stock to ascertain whether others have claims on the same item of equipment.

Attracting private capital

Creating enhanced security will draw more private capital into the African rail industry, at more attractive rates, without the need for state guarantees, thereby reducing dependency on government and donor funding, and facilitating investment on an economic basis, when business conditions dictate, not when there is room in the state budget. So it should be: just because governments finance the building of the roads, that does not mean that they should own or finance the cars running on them.

Just as important, the limited second user market in rolling stock will receive a significant boost, as the Protocol makes operating leasing a much more viable business option, thereby lowering barriers to entry into the industry for private sector rail operators, and making existing operators more efficient and competitive.

Railways will be the key to successful (and environmentally sustainable) transportation of both people and freight, both across the continent and within local suburban areas; the most efficient method of transporting commodities to ports is by rail. There is no question that a more effective rail network across Africa will be vital to its development.

The Luxembourg Protocol has the potential to be the solution to a significant problem in the African railway industry. It will allow governments to focus on infrastructure development and leave financing the equipment and rolling stock to the private sector.

It is not yet in force, but has already been signed by one African government and more signatures and ratifications will come soon if the industry asks for them – and it is imperative that it does so. Too many trains have gone on well beyond their useful life or are “retired” without replacement. In future, if the Protocol is adopted, trains will have gone, not to the scrapyard, but to the next station and beyond. It is an opportunity which should not be missed.

Howard Rosen is an English lawyer based in Switzerland, specialising in transportation finance (www.legalease.ch). He also chairs the Rail Working Group (www.railworkinggroup.org) dedicated to the implementation of the Luxembourg Rail Protocol.