



# Merced – Bakersfield Interim Service Proposal

Finance & Audit Committee  
Business Case Assessment Study  
Update

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# Introduction

The KPMG financial advisor team has been engaged in developing a Business Case Assessment Study for the proposed Merced to Bakersfield Interim Service, from June 2019 to October 2019

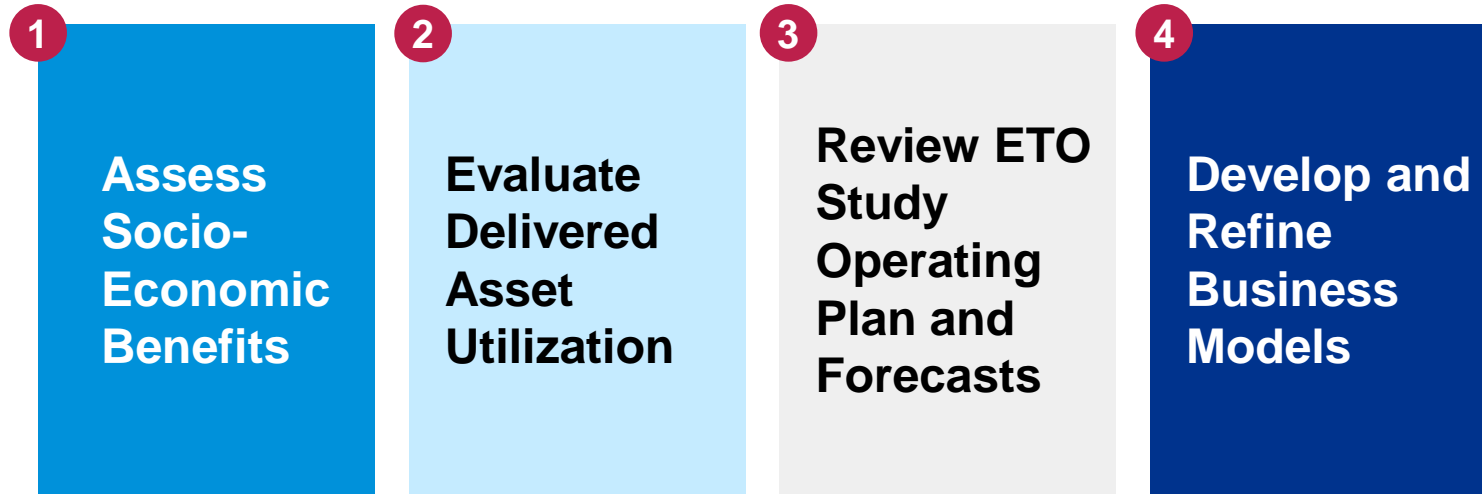


## Historic Overview

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- **January 2018:** The Authority identified cost and schedule impacts that compel a review of program capacity within revised budget constraints
- **June 2018:** As part of its 2018 Business Plan, the Authority initiated planning / analysis steps related to early use of Central Valley infrastructure / this was driven by an identified funding gap for completing the Valley to Valley
- **May 2019:** As part of the 2019 Project Update Report (PUR), the ETO published its operations and financial plan study of the Central Valley and Peninsula corridors interim service
- **May 2019:** The PUR recommends developing interim high-speed rail service between Merced and Bakersfield as the first building block of the Valley to Valley Line. Governor Newsom endorsed the Building Block approach to delivering the high-speed rail system.
- **Late May 2019:** KPMG is engaged by the Board's Finance and Audit Committee to conduct a Business Case Assessment Study for the proposed Merced to Bakersfield interim high-speed rail service

# Business Case Scope Elements



# 1 Socio-Economic Analysis

**Purpose:** Evaluate the broader community and regional benefits from additional investments in California's Central Valley

- Conducted interviews with staff from the Authority's Business and Economic Branch
- Reviewed Authority's economic impact analysis methodology
- Reviewed Authority's emissions reductions methodology
- Reviewed California State Auditor Report findings on Authority's socio-economic studies
- Reviewed the Authority's new Merced-Bakersfield analysis
- Conducted gap analyses on economic impact components

## 2 Asset Utilization Evaluation

**Purpose:** Assess the feasibility and rationale for interim usage of High-speed rail infrastructure, prior to the introduction of full Valley to Valley High-speed rail service

- Reviewed language in federal and state funding plans and agreements
- Held discussions with Authority staff and external stakeholders such as the San Joaquin Joint Powers Authority (SJJPA), San Joaquin Regional Rail Commission (SJRRC), and CalSTA
- Analyzed the risk of unutilized completed assets before the completion of the Valley-to-Valley
- Reviewed potential mitigations of this risk through interim service

## 3 ETO Study Operational Review

**Purpose:** Review the rationale and reasonableness of assumptions in the proposed operating plans used for Ridership and Operations and Maintenance (O&M) forecasts

- Discussed with the Early Train Operator (ETO) and the state rail ridership team (CalSTA)
- Reviewed assumptions contained in the ETO study, as well as supporting tech memos
- Conducted review of ETO operations & maintenance cost model
- Provided initial findings to ETO for further review and comment

## 4 Business Model Development

Status: Analysis Completed

**Purpose:** Assess potential business models and commercial agreements for Merced to Bakersfield interim service

- Held discussions with key stakeholders such as CalSTA, DOF, SJJPA, and SJRRC
- Analyzed different business models that could be used for the Merced to Bakersfield interim service
- Identified 2-3 options for further consideration
- Based on Authority feedback, identified preferred business model

## 5 Capital Program Affordability Analysis

Status: Analysis Completed

**Purpose:** Understand how the Merced to Bakersfield construction cost estimates align with the Authority's anticipated revenues and existing funding sources

- Performed analysis to determine whether funding deficits are anticipated
- Reviewed the Authority's capital cost forecasts and schedule (P70 and P90), in comparison with projected funding sources
- Developed four program funding scenarios reflecting the same assumptions used in the 2019 Project Update Report
- Conducted a risk review on both funding and capital program



## 6 Stakeholder Investments Review

Status: Analysis Completed

**Purpose:** Assess stakeholders' current and future plans for Central Valley connectivity, which would support Merced to Bakersfield interim service

- Held discussions and interviews with stakeholders in order to assess connectivity plans and the need / structure for potential partnership agreements
- Discussed investment and funding requirements to achieve the stakeholders' proposed capital program
- Reviewed capital and business plans proposed by stakeholders in order to determine alignment with Authority operating plans
- Compared stakeholder infrastructure plans with those assumed in the ETO Study

## 7 Return on Investment Analysis

**Purpose:** Evaluate the financial return from delivering the Merced to Bakersfield service as a part of the Authority's current Valley to Valley plans

- Conducted new financial analysis and built discounted cash flow model to measure the potential return on investment of the Merced Extension
- Analysis was conducted on the incremental value of adding the Merced Extension to the existing V2V IOS scenario, as an extension of the 2018 Business Plan analysis
- Coordinated with ETO on required ridership, revenue, and O&M scenarios for the analysis

## 8 Long-Term Contracts Impact

**Purpose:** Assess the impact of Merced to Bakersfield interim service on current contracts and future planned procurements

- Held stakeholder discussions regarding the implications of interim service on track & systems and rolling stock procurement packages
- Assessed impact on procurement schedule
- Reviewed key assumptions for interim service in order to assess procurement scope adjustments
- Gathered information on operating risk transfer, capital maintenance cost liability, and contract management and oversight responsibilities

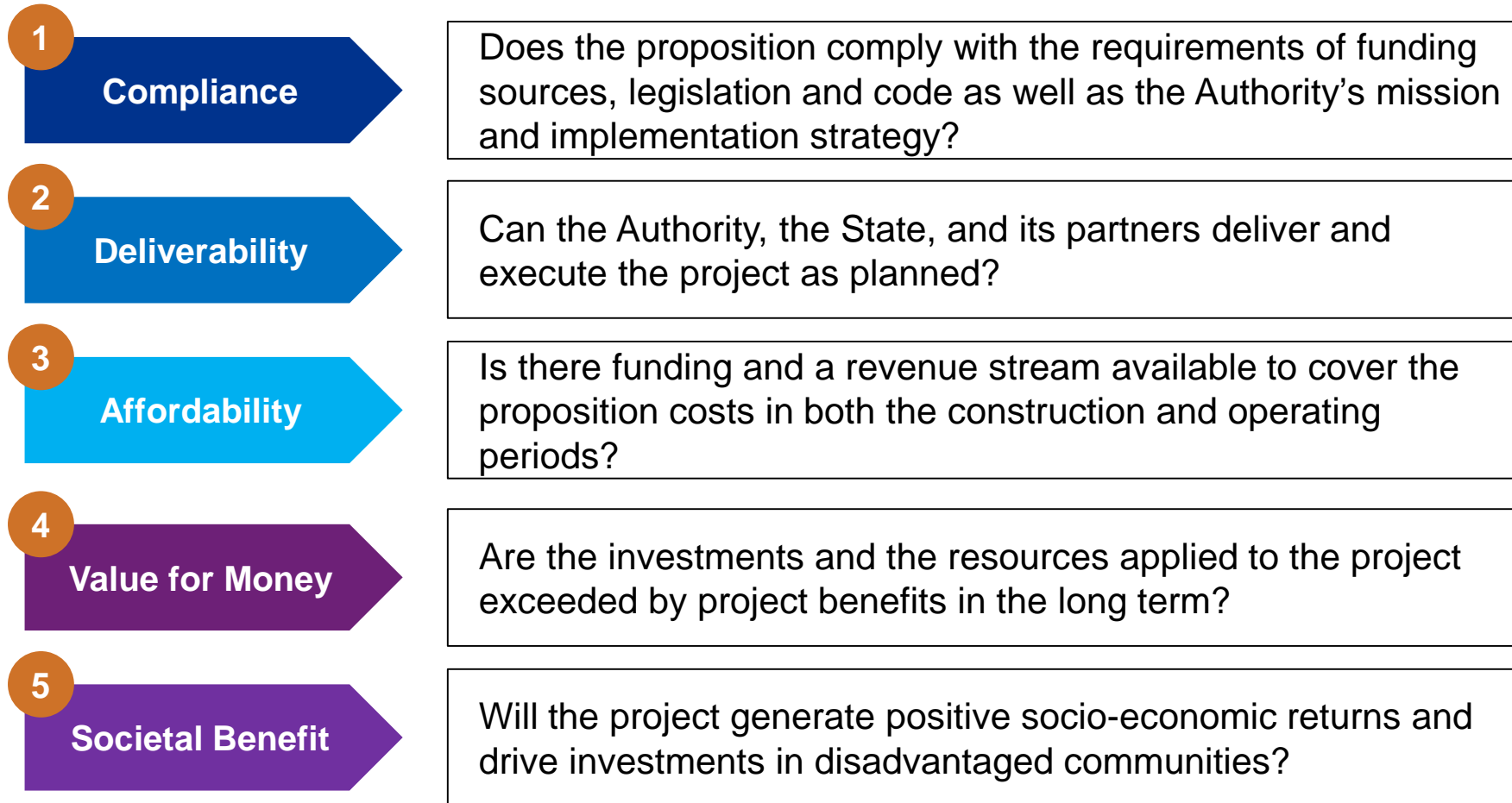
## 9 Risk / Mitigation Evaluation

**Purpose:** Document the potential risks from delivering Merced to Bakersfield interim service and identify potential mitigation steps

- Conducted interviews and meetings with stakeholders and Authority staff on interim service risks
- Identified major risks and potential mitigations for interim service
- Discussed potential mitigation strategies with Authority staff

# Key Decision Factors for Decision Making

The analysis viewed interim service through the lens of five decision factors aimed at supporting decision makers



## Preliminary Key Observations (1/2)

### 1. Investments are Expected to Deliver Socio-Economic Benefits

- 30% forecast increase in job-years and \$9.2 billion in overall economic activity
- Benefits will positively impact disadvantaged businesses and communities
- Other benefits related to safety, noise, travel times, emissions, and congestion relief

### 2. Interim Service Allows Early Utilization of HSR Infrastructure

- Reduces risk of unutilized assets prior to the completion of the Valley to Valley system
- Allows for revenue generation in order to cover maintenance and security costs
- Allows Californians to take early advantage of HSR service

### 3. Merced to Bakersfield is Affordable Under Base Case Scenario

- Current capital cost estimates at \$20.4 billion (YOE dollars)
- Current projected funding of \$20.6 billion to \$23.4 billion (YOE dollars)
- Affordability is dependent on economic conditions and cost estimates remaining stable

## Preliminary Key Observations (2/2)

### 4. Positive Return on Investment from Merced Extension

- Estimated incremental discounted cash flow of \$700 million to \$1.1 billion through 2060 if the Merced Extension (with a partial Wye) is built as part of the Valley-to-Valley system
- This estimate factors in projected revenues, operating expenditures, and capital costs

### 5. Aligns with Future Track & Systems and Rolling Stock Procurement

- Procurement packages included long-term and complex provisions that would accommodate interim service
- Structured to allow flexibility on segment commencement dates through multiple Notice to Proceeds (NTP) allowing alignment with Building Block approach

## Next Steps

- Review revised ETO study / analysis (e.g. ridership, costs data, and financial results)
- Prepare recommendations addressing Merced and Bakersfield extensions, and interim service
- Finalize risk and opportunities assessment using decision factors
- Finalize business case





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