

ON THE IMPACT ON THE STATE OF SERVICING DEBT ON THE 'ENTIRE SYSTEM' Brief Note # 19 – August 16th 2011

From the authors of *The Financial Risks Of California's Proposed High-Speed Rail Project*, six subsequent Briefing Papers, and *The Financial Analysis of Proposed CHSR Project*. Available at www.cc-hsr.org

Finding: The inability of the high-speed rail's operating margins to produce sufficient cash to service the construction debt (interest and principal repayments) might require additional State debt. This would lead to the State's debt servicing obligations exceeding 10% to 16% of General Fund Revenues over the next twenty years unless taxes are significantly increased.

Background: The State's Treasurer and the Legislative Analyst's Office (LAO) periodically make long-term forecasts of the State's debt servicing obligations as a percent of the General Fund's projected revenues. The last forecast was completed in late 2009.¹ It included the impact of the Prop 1A debt servicing obligations, but did not address the impact of additional construction debt having to be serviced from the General Fund. Estimates now show there are insufficient operating margins in the HSR program to cover all of the debt servicing obligations of the construction debt.²

The table to the right shows the magnitude of the problem. In Section (A) the 'Current Estimate' row shows the Treasurer's and the LAO's forecast of all debt servicing such as \$15.3Billion in 2030.³ If the 'Entire System' (all 6 cities) of the high-speed rail program achieves 100% of its operating margins, there will be \$3.8Billion in additional debt service obligations that cannot be covered by its operating margins, raising the State's annual obligation in 2030 to \$19.1Billion. If the high-speed rail program has no operating margins to contribute to servicing construction debt, the State's obligation will increase to \$23.3Billion per year.

Impacts On The General Fund From Debt Servicing The Construction Debt Of California's High-Speed Rail Project					
Budget Year - FY	2010	2015	2020	2025	2030
(A) Debt Service - in \$Billions					
Current Estimate	\$6.8B	\$10.0B	\$11.7B	\$14.0B	\$15.3B
Plus HSR at 100% Plan	\$6.8B	\$10.7B	\$15.9B	\$19.0B	\$19.1B
Plus HSR at no Op Mar	\$6.8B	\$10.7B	\$16.3B	\$21.7B	\$23.3B
(B) Debt Service, % of General Fund Revenues, assumes Treasurer's 5.3% annual growth rate					
Current Estimate	7.8%	9.0%	8.0%	7.5%	6.6%
Plus HSR at 100% Plan	7.8%	9.6%	11.0%	10.1%	8.2%
Plus HSR at no Op Mar	7.8%	9.6%	11.2%	11.5%	10.0%
(C) Debt Service, % of General Fund Revenues, assumes a lower 3.0% annual growth rate					
Current Estimate	7.8%	10.2%	10.3%	10.7%	10.3%
Plus HSR at 100% Plan	7.8%	11.0%	14.0%	14.5%	12.9%
Plus HSR at no Op Mar	7.8%	11.0%	14.3%	16.5%	15.7%

Section (B) displays these projections the same way the LAO displays future obligations, as a percent of the projected General Fund revenues. The current General Fund revenue projection from the Treasurer's Office is based on an annual revenue growth rate of 5.3%. The three rows in Section (B) show the projected debt servicing obligations as a percent of these revenue projections. However, if the State's revenues grow more slowly, say 3% annually, debt servicing obligations as a percent of General Fund revenues will be much higher, as shown in Section (C).

Conclusion: If the worst case's conditions materialize; that is if State revenues only grow by 3% annually, and the HSR program fails to contribute any operating margin to pay off the construction debt, the total State's debt service could be in the range of 15% to 16% annually of General Fund revenues within 10 to 15 years. Of this obligation, the impact of the high-speed rail program will be about one third of the total annual obligation. It will be very difficult to fund other State priorities such as education, safety or other transportation initiatives without higher taxes to reduce the debt load created by the 'Entire System's' inability to service all of its construction cost debts.

¹ Treasurer's Office *Debt Affordability Report*, October 2009, pages 7 and 8. See: <http://www.treasurer.ca.gov/publications/2009dar.pdf>
Also, LAO, *Informational Hearing on Debt Service*, December 2009, page 3. See: http://www.lao.ca.gov/handouts/FO/2009/Debt_Service_121409.pdf

² *Financial Analysis Report*, June 2011, and Briefing Notes #16 and #17, August 2011. All available at www.cc-hsr.org

³ Bonds Already Sold, plus Authorized But Not Yet Sold, plus Projected Future Authorizations (excluding high-speed rail).