



## Cadiz aligns the incentives as momentum grows behind water project

The controversial water supply initiative is raising capex in the hope of delivering first water by 2026. Is it finally a case of ‘right place, right time’?



### Kennedy walks the walk

CEO Susan Kennedy has successfully parlayed her political pragmatism to advance the Cadiz water supply project to the brink of execution.

Cadiz, Inc.

Shares in Nasdaq-listed Cadiz Inc. have risen by 30% over the last three months after the market drastically reappraised its relationship with the company in light of the progress made under CEO Susan Kennedy.

The signing of a series of supply agreements has strengthened the belief that the company is finally in a position to raise the \$800 million of capex it needs to complete the conveyance infrastructure necessary to deliver water from the aquifer underlying the acreage it owns in California’s eastern Mojave Desert.

“We have the infrastructure to move the water, and we’ve got 20 years of permitting and litigation in the rear view mirror,” Kennedy told GWI this month.

“In the first quarter of this year, you saw us announce the first 40- and 50-year contracts for water supply with public agencies. Cadiz is now at an inflection point that politically just didn’t exist two years ago, and we now have a corpus of take-or-pay contracts for water supply at a price point that allows us to go and finance the infrastructure.”

When Kennedy was parachuted into the CEO role in 2021, she arrived with an enviable resume of political negotiating experience. As chief of staff to Governor Arnold Schwarzenegger and cabinet secretary to Governor Gray Davis before that, she was on the front line of the energy and water debate at the state

level. She also served on the California Public Utilities Commission, which gave her an intimate understanding of how utility infrastructure operates.

Before Kennedy joined the company, the Cadiz project had reached a point where it was viewed as so toxic politically that it was proving difficult to convince any water agency to sign a deal with the company – no matter how badly they needed the water.

“The politics around water have shifted dramatically in the last three years,” Kennedy observed. “The water infrastructure in California was built around a very predictable set of hydrological conditions. All of our water infrastructure was built around snowmelt in the mountains, and climate change means that it’s now falling as rain. It doesn’t matter how much money you put on the table, you can’t build water infrastructure to deal with this problem fast enough.”

That is where the Cadiz project comes in. The company holds permits to export an average of 50,000 acre-feet per year (168,973m<sup>3</sup>/d) for 50 years from the aquifer under the land it owns, and is also permitted to import 1 million AF of non-native water.

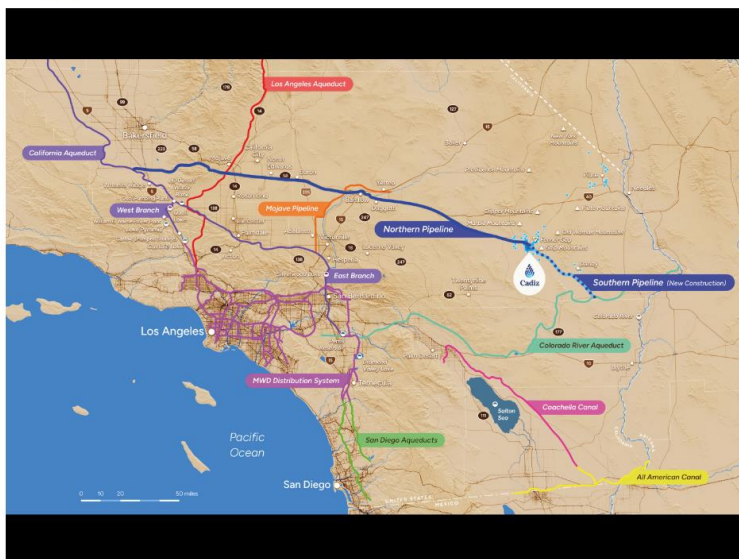
“Having a fully capitalised water bank located between the Colorado River system and the State Water Project is what makes this a super valuable asset. Having water already in storage allows us to maximise the revenue streams available, and based on our current permits, we estimate we can generate more than \$5 billion in cash flows from the water assets over the life of the project,” Kennedy explained.

The key pre-requisite to putting the project finance package in place is getting firm commitments from offtakers, and in June, the company signed a 50-year take-or-pay agreement with Santa Margarita Water District to deliver 5,000 acre-feet of water per year to groundwater banks located along Cadiz’s 220-mile Northern Pipeline (see map below).

#### SMART NETWORKING: HOW WILL CADIZ PLUG INTO SOCAL'S WATER SYSTEM?

The Cadiz water supply project has been 40 years in the making. The infrastructure and permits are there, but can it raise the capital it needs to start delivering water?

Source: Cadiz, Inc.



“The agencies that need firm contracts are those that have limited access to groundwater, limited access to recycled water, and are facing cutbacks on their Colorado and State Water Project supply,” said Kennedy. “If I didn’t have those water contracts, I couldn’t attract the equity investors.”

The deal will utilise a master limited partnership (MLP) structure – believed to be a first in the water sector – whereby Cadiz, as the general partner, will contribute all the physical assets, including the pipelines and the rights-of-way permits for the Southern Pipeline, while the limited partners in the MLP will put up the construction finance. They will then be entitled to 51% of the revenues from operating the storage bank by charging wheeling fees to the recipients of the water.

“The MLP model is low-risk and high-return. Cadiz will retain the revenue stream from the sale of the water supply, and the MLP would come in and own the infrastructure assets. The LPs will get a per acre-foot year fee for moving water through the pipelines,” she explained.

Perhaps Kennedy’s shrewdest move has been to donate surplus water not contracted under take-or-pay agreements to disadvantaged desert communities, giving them a clear incentive to apply for grant funding in order to fund the pipeline infrastructure that will enable the water to be conveyed to their communities.

“I started signing up tribal nations and farm worker communities by saying: ‘I’m giving you the water now, which means you have a vested interest in helping to apply for the grant funding that will cover the capex. In addition, some Native American tribes have deep pockets from gaming revenues, and counties have pension funds that would love to invest in infrastructure that has a stable return. As long as I have the core equity capital from these public entities, I can match that with grant funding. We think that a minimum of 50% of the infrastructure costs can be covered by grants.’”

By structuring the project in this way, Kennedy has skilfully maximised the incentive for different groups of stakeholders to get involved.

“We now have the right entities in place that have a vested interest in owning and operating the infrastructure. It’s the ‘have-nots’ that are going to attract the grant funding to finance the infrastructure, while the ‘haves’ are going to pay them a tolling fee to use their infrastructure to move water to their communities. We’ve flipped the entire utility business model on its head,” she told us.

Cadiz has capped the total out-of-pocket cost of supplying water from the aquifer at \$1,650/AF (\$1.34/m<sup>3</sup>), which includes the pro rata capital cost to end users of constructing local delivery infrastructure, and the operating cost of getting the water to where it is needed. Kennedy believes that this should allow the project to be cost-competitive with the current rates charged by the Metropolitan Water District of Southern California.

Once the pipelines come online, those users receiving donated, ‘tier two’ water from the project will only have to cover the energy bills to convey the water to their communities, meaning the unit cost to them could end up close to the \$250/AF that Metropolitan was prepared to pay 20 years ago to access the entire 1 million acre-feet of storage capacity in the Cadiz project. Negotiations on that

deal collapsed after politics resulted in the plug being pulled, based on the argument that access to additional water supplies would act as a growth catalyst and cause environmental damage by creating housing developments on pristine desert land.

“For 20 years, this project was persona non grata,” Kennedy remembers. “They tried to kill it by litigating the pumping rights, but they couldn’t provide any evidence of environmental harm, which means that the permits for pumping around our project are bullet-proof today.”

The 220-mile buried Northern Pipeline still needs to be repurposed for water conveyance by constructing pumping stations and offtake points before it is ready to start delivering water into the Southern California distribution network.

“Our target is to be in construction in 2025, and to be delivering water in 2026 from the Northern Pipeline,” said Kennedy. “Simultaneously, we will finish the engineering and the permitting for the storage project on the Southern Pipelines, with a target to be delivering water in 2027. It’s a new-build project, but it’s mostly downhill, so it’s going to be very cost-effective in terms of delivering water. It’s a story of right place, right time, and that’s what I’m so excited about.”