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SHALE GAS— BOOM OR BUST

By Ed Berghard

A Quick Look At The Barnett Shale Economic Impact

CONGRATS TO NEW SAN DIEGO EDC PRESIDENT & CEO

Mark Cafferty, a longtime San Diego community leader of the area's workforce program has been named to succeed interim President, Bill Geppert and retired Julie Meier Wright as the next President & CEO of the San Diego EDC.

In Julie's final year at the helm, she led a significant program shift to focus on global business development into the region, which includes San Diego County and Cali Baja. KMK Consulting is proud to be a trusted advisor to this successful leadership organization.

America's Appalachia Region is home to roughly 23 million people. And, despite having abundant natural resources, the Region's history is associated with persistent poverty. In the early 1900's the logging and coal mining industries created good paying jobs, but the Region failed to leverage the benefits of the economic "Boom" and suffered through a prolonged "Bust" as capital investment in and production from these industries has declined. Failure to capitalize on the "Boom" to create sustainable economic prosperity is a reflection of limited vision and poor strategic planning by local community leaders. And now, the Region is again faced with an opportunity for economic growth stimulated by commercialization of another abundant natural resource – the Marcellus and Utica shale gas reserves.

The Marcellus Shale formation is 400 million years in the making and lies under Maryland, New York, Ohio, Pennsylvania and West Virginia. The Utica Shale formation is 40 – 60 million years older. It is 3,000 – 7,000 feet under the Marcellus and extends to even larger section of the Appalachia Region. Geological surveys predict these two formations combined have the potential to produce
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This fall, the Ft. Worth Chamber issued a study prepared by the Perryman Group summarizing the impacts from a decade of drilling in the region. Just highlighting some statistics from this study helps to put in perspective the substantial economic impact related to the energy shale industry:

- Over the past decade the Barnett Shale's cumulative economic impact includes \$65.4 billion in output for the region and \$80.7 billion in output for the state.
- Approximately 38.5% of the region's economic growth since 2001 stems from the Barnett Shale activity. This constitutes roughly 8.5% of the local business complex of Fort Worth.
- The Barnett Shale has yielded 9 Trillion cubic feet of natural gas since 2001.
- In 2011, the Barnett Shale activity will generate \$11.1 billion in annual economic output.
- Activity in the Barnett Shale has created 100,268 jobs in the region and more than 119,200 jobs throughout Texas.
- Salaries and wages in North Texas are 8.7% higher than they would be without the Barnett Shale business.
- Local taxing entities have received approximately \$5.3 billion in tax receipts from Barnett Shale activity over the past 10 years while the state has received \$5.8 billion.

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DON'T SETTLE FOR INCUBATORS WHEN YOU CAN HAVE ACCELERATORS

Everywhere you turn, the latest and greatest economic development strategy is focused on entrepreneurship growth. There are lots of reasons why this has become somewhat the obvious central theme of many business plans of many communities. What the Ewing Kauffman Foundation in Kansas City envisioned 20 years ago, has finally taken over as one of the most important building blocks of job growth and prosperity building in communities across our land.

While incubators are still very relevant and in most places are still very popular and effective, it seems that every community has or is starting at least one accelerator. In the Cincinnati market, there are now three. Of these, two are specifically crafted to attract startup businesses from across the country into this region on both sides of the Ohio River. Each is focused on a particular target industry, the one in downtown Cincinnati being consumer branding and the one associated with Northern Kentucky University being Informatics. The Cincinnati market also has two life science incubators plus two others, considered to be general technology incubators. While this may seem to some as an overcrowding of support structures to spawn entrepreneurial startups in a market the size of Cincinnati, indeed, that is not the case. All of these can survive, all of these can make a meaningful impact on entrepreneurship critical mass for the Cincinnati market.

The oldest of the three accelerators can be found at CincyTech USA led by its President Bob Coy. This organization has been eminently successful, having realized perhaps its largest payday success last spring, supporting the startup and then participating in the exit sale of Blue Ash Therapeutics, sold to a New York company. Cincy-Tech also just invested in its 30th portfolio company which relocated from L.A. The two newer accelerators, however, offer a much different set of participation rules of engagement in an effort to try to keep their startup companies growing in Cincinnati as long as possible. The downtown Cincinnati accelerator called The Brandery has now been through its first graduating class. It is headed by Mike Bott, who is expecting 300 applications from across the country this spring for 10 places in its intense 12 week summer program. (continued, *Don't Settle*, page 4)

DOES TOP TIER CEO LEADERSHIP REALLY MATTER FOR A COMMUNITY'S ECONOMIC DEVELOPMENT SUCCESS?

This is, of course, a rhetorical question. Any community that needs to ask this question seriously, is behind the curve and it needs to play catch-up.

KMK Consulting has specialized in building these leadership structures around the country for about the past 10 years. The leading best of class model continues to be found at the Metro Orlando Economic Development Commission. The success of that CEO Group, known as the Governors Council, has been instrumental in transforming Orlando into a legitimate and competitive business destination. Paradoxically, the impetus for this organization came from tourist juggernaut Disney World and its then CEO, recently retired, Allen Weiss. Since its founding, the unified horsepower of those CEOs has had an outstanding track record of success capped by the recruitment of the Sanford Burnham Medical Research Institute to be the anchor of a game changing development known as Medical City at Lake Nona located on the outskirts of Orlando's Sanford International Airport. For the many inside and outside of Florida wondering how Orlando does it, look no farther in the Governors Council. While we have had the honor of building these organizations in communities from the East to West Coasts of the country, involved from their original conception to CEO recruitment to agenda crafting, and performance, each one has its unique characteristics. They have different membership requirements, different sizes, different scopes of work and different metrics. But they all share the same core critical underlying theme. Specifically, the best agendas, the best implementation, the best successes in economic growth are underpinned by a community's top tier private sector leaders. This level of leadership engagement is not delegable if maximum impact is the objective.

This core principle might be easy-to-read or easy to say, but making it happen successfully in a given community in a sustained manner is what differentiates best of class, best of competition and what constitutes a big part of KMK Consulting's reputation.

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GROWTH IN NEW MARKETS TAX CREDITS – *A financing tool no community can afford to miss.*

As the New Markets Tax Credit (NMTC) conference wraps up in San Diego following two days of dynamic discussions, this major economic financing tool continues to grow in impact at the federal level and now also at the state level.

Through Fiscal Year 2010, community development entities (CDEs) dispersed a total of \$20,901,020,746 in qualified equity investment (QEI) proceeds to 3,060 qualified active low income community businesses (QALICBs) that financed both real estate development and operating businesses in low income communities. Just in Ohio, for instance, there was over \$1 billion in private capital investments that the NMTC program attracted to Ohio businesses between 2004 and 2010. Under any analysis, over any timing metric over the past 10 years of the life of this program, it has been nothing less than a huge economic development success in redeveloping neighborhoods and central business districts in every community that has taken the time to learn and to compete within the strict rules of this Clinton era initiative.

And now, as the federal NMTC program goes into an extended life thanks to legislative action, the program is being adopted at the state level as well. For example, on January 4, 2012 California Assembly Bill 643 proposed the creation of the California New Markets Tax Credit Program. This bill would authorize a California tax credit allocation committee to grant up to \$50 million in state NMTC's each year from 2013 through 2019 to stimulate economic development and hasten California's economic recovery. Qualifying investments include retail businesses, real property, financial institutions and schools, among others.

The following week, Indiana state representatives introduced H.B. 1248 to create its New Markets Job Growth Tax Credit. This program would provide a state tax credit equal to 39% of the purchase price of a qualified investment, limited to \$10 million per transaction. H.B. 1248 also provides for a \$20 million annual cap and a five-year carry forward period. If enacted, the program would take effect in 2013. More of this kind of state legislation is certain to follow. (continued, *Growth in New Markets*, page 4)

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In the case of Orlando, many of the CEOs were already involved to some degree with the economic development program. But a more dramatic example of the power of these types of structures can be found down the road in Fort Lauderdale. The CEO Council of the Greater Fort Lauderdale Alliance is just starting its fifth year and is the Who's Who of Broward County power players including Wayne Huizenga and AutoNation Chairman & CEO, Mike Jackson. Most of these CEOs were not involved at all in what was called the Broward Alliance. Their focus has been to put Fort Lauderdale and Broward County on the map for small to medium size company headquarters. Ask any site selector involved in Florida and he or she will attest that this CEO Council, led by Robin Ronne, is a big winner producing deal flow, relocation of headquarters and an 82% awareness of Fort Lauderdale as having a very positive image. The group has been so grateful to their Chairman, Ray Ferrero, Jr. that this past October they inaugurated an annual leadership award in his name.

These initiatives work. They can be game changers. In some communities they can be the secret weapon.

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(Barnett Shale, continued from page 1)

- Barnett Shale and related activities generate roughly \$730 million in additional revenues annually for North Texas counties, cities and school districts.

So energy shale, at least certainly in Texas, is indeed big business with very significant economic impact. But even it is subject to cutback as is currently happening in Texas, responding to low-pricing of natural gas. As Ed Burkhard in his lead article has said, this business demands huge attention from economic development professionals and their organizations.

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While accelerators like The Brandery have found success in attracting startups, even from outside the United States, with grants of \$20,000, the Northern Kentucky Informatics accelerator called UpTech intends to go much further dangling grants of \$100,000. Their goal is 50 new businesses, each with one of these grants over the next 3 to 5 years. The 30 day application process for the first group of 10 is this month of February. In addition to this attention-getting six-figure grant, the caliber of the judges is equally as impressive coming from companies like Cisco, Dell, Procter & Gamble, SAP and Scripps.

The other great spinoff benefit from these accelerators is the buzz that they are creating across the community. Pretty much every organization involved in any capacity in the economic development delivery system process in the Cincinnati market is on board this collective entrepreneurship mission from major corporations, foundations, Chambers of Commerce, universities, banks and, of course, all of the city's leading law firms. This buzz, this collective entrepreneurship effort, also plays an important part in the Cincinnati market's effort to enhance the lifestyle and attractiveness for young professionals, whether they be startup company founders or new Procter & Gamble recruits from around the world.

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Indeed, the best thing to do in every community is to learn the rules. The best way to do that is to follow the experience of experts who have been down this road many times already. The best authority is Novogradac and Company LLP. Their New Markets Tax Credit Resource Center is the a great way to learn and stay current with highly competitive programs. See www.novoco.com.

Another avenue is to follow the experience of folks like the NMTC deal team at Keating Muething & Klekamp PLL. This team has extensive experience representing not only the CDE, but also the borrower, known as the QALICB as well as the tax credit investor and senior debt provider, usually a bank or a life insurance company. While this KMK group has been counsel to over \$150 million in NMTC transactions in Cincinnati, they have also recently completed transactions from Brunswick, Maine to Mount Olive, Mississippi and Birmingham, Alabama.

New markets tax credits are complex and usually foreign to most borrowers as well as to many communities and their economic development organizations. This KMK team prides themselves in helping to educate borrowers, lenders and communities on how NMTC's can help meet client needs, restore communities and build prosperity and jobs.

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enough natural gas to meet U.S. demand for generations.

In towns throughout the Appalachia Region, like Williamsport, Pennsylvania, people are seeing the early “Boom” benefits of commercializing shale gas. New jobs and renewed hope for a prosperous future are evident. As you’d expect, with the emergence of any new industry there are several unknowns to address. In the case of shale gas, commercialization is raising important questions regarding appropriate stewardship of natural resources like water and air as well as the potential impact on seismic activity in the Region.

But, given the “Boom-to-Bust” track record of the Appalachia Region, one question that needs to be asked is – “How can the Region leverage this opportunity to create sustainable economic prosperity?” The answer is by creating and deploying effective local community strategic plans that are 10 – 15 years in horizon and recognizing the non-renewable nature of this energy supply source. Economic development professionals in communities impacted by shale gas commercialization have a unique responsibility to catalyze the creation of such plans.

It is important to understand, that while the industry will be viable in the Region for 50 plus years, at the community level a well may only be commercially viable for 10 years or less. History makes it clear that failure to provide appropriate stewardship of a community’s economic portfolio and infrastructure will result in an inevitable “Boom-to-Bust” cycle that will leave the citizens economically and emotionally worse off than before the drilling started.

Creating an effective long-term strategic plan for a community is never an easy challenge under the best of circumstances, let alone faced with a transformational tidal wave like shale gas commercialization. But, it is certainly not an impossible task. The majority of community impacts are predictable. And if you can see the “rocks in the river”, you can navigate around them.

The challenge is that most small communities that will be impacted by shale gas commercialization do not have adequate experience, staff or resources to deal with the foreseeable changes if they operate on a “business as usual” basis. Local economic development (*Shale Gas*, continued page professionals need to provide planning support to their community leaders.

It starts with ensuring a common understanding of the practical challenges your community will face when the drilling phase begins. These include, but are not limited to, social impacts (rapid increase in population, increased crime rate, increased stress on emergency services, increased demand for housing, traffic jams, higher prices in stores, outsider influence on local culture, community education), and infrastructure impacts (unplanned and unbudgeted road repair, demand for increased government services and staff, need for ensuring local and state regulation compliance, demand for educational services, need for skilled labor).

It also includes preparing for when the industry leaves the community. That means collaborating with local public and private sector leaders on creating a sustainable future vision for your community. It means enrolling academia to help ensure an adequate skilled labor pool to support the shale gas industry in the growth phase and a retraining effort to ensure employability of idled labor when the industry leaves. It means initiating an aggressive effort to attract capital investment from adjacent industries so you minimize the risk of experiencing an economic “Bust” by diversifying the industry base in your community before the shale gas industry has reached its peak impact. It means making smart choices about infrastructure investment so your community is not saddled with long-term debt in the face of a dramatically reduced tax base.

Local economic development organizations need to understand the scope of resources available from regional and state government as well as the industry itself, and how to tap into them for help. If a community wants to not only survive, but also thrive from the impact of shale gas commercialization it needs to leverage all resources available.

Luckily for communities in the Marcellus and Utica Shale reserves, there is a lot that can be learned from communities in more developed shale reserves like the Barnett Shale Reserve (Texas), Woodford Shale Reserve (Oklahoma), Haynesville Shale Reserve (Louisiana) and Fayetteville Shale Reserve (Arkansas). There is also a lot to be learned from academic studies. Some of the leading academic experts include Dr. Susan Christopherson (Cornell University), Dr. John Curtis (Colorado School of Mines) and Dr. Diane McLaughlin (Penn State University). These experts are actively studying the social impacts of shale gas commercialization on communities and documenting best practices for dealing with the challenges. (*Shale Gas*, continued page 6)

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In addition, the Strengthening Brand America Project has information for economic development professionals providing advice on how to think about and manage the local economic impact of the shale gas industry (<http://strengtheningbrandamerica.com/blog/category/shale-gas/>). In 2012, the Project will be expanding its support of economic development professionals in affected communities by creating a special area that focuses on providing best practice case studies and guidance on effective strategic planning.

Will the Shale Gas industry turn out to be a springboard to sustainable economic prosperity or is the Appalachia Region destined to repeat the historical pattern of “Boom-to-Bust” that has dogged it throughout the 20th century?

I have no doubt that the questions around environmental stewardship and industry regulation will be satisfactorily addressed. It will take time and the debate will likely be vigorous and confusing at times. But, it will be figured out and regulations will be established to protect both the industry and environment.

I am hopeful the need for effective long-term strategic planning at the local level is recognized by community leaders and made a top priority. The fact that shale gas commercialization will have a transformational impact on any community it touches is absolutely clear. However, the more relevant question is whether communities will accept their role and responsibility to chart a future that ensures citizens are better off after the industry leaves than before the drilling started.

In my opinion, a key to success is how well local economic development professionals do their job. These professionals are uniquely positioned to lead their community leadership and help ensure proper strategic plan design and deployment. Leading leaders is always difficult. Congratulations in advance for those who successfully rise to the challenge.

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