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Shale Oil & Gas Industry Update

SHALE INDUSTRY: INDUSTRIAL REAL ESTATE AND CONSTRUCTION SECTOR TRENDS IN OHIO AND NATIONALLY

KEY FINDINGS (DETAILED BELOW):

- Local governments' efforts to raise revenue through sale of mineral rights present opportunities -- and risks.
- The industrial real estate and construction sectors will continue to be driven by an influx of businesses providing oil and gas support services, particularly along the axis of new exploration -- though it's too early in the cycle to know how deep, or long-lasting, the shale boom will be.
- Shell and TravelCenters of America are betting on natural gas fueling the transportation sector.
- The next wave of development is likely to include plastics and chemical manufacturing.
- There are competing estimates of economic benefits of shale gas production.
- Nationally, broad indicators point to modest growth in real estate and construction sectors, driven by shale and manufacturing. At the same time, a decline in activity funded by the government's stimulus plan will provide some counterweight to that growth.

OHIO TRENDS AND ISSUES IN SHALE-RELATED REAL ESTATE AND CONSTRUCTION

Local governments are seeking to sell mineral rights for lands they own.

The city of Youngstown is reportedly investigating its options for selling the mineral rights on lands it owns. It would be following the lead of Campbell and Struthers, nearby cities that have recently announced their own plans to sell their mineral rights. Youngstown's Mayor says that he hopes to use the funds from such a sale to pay for demolitions, redevelopment and other improvements.

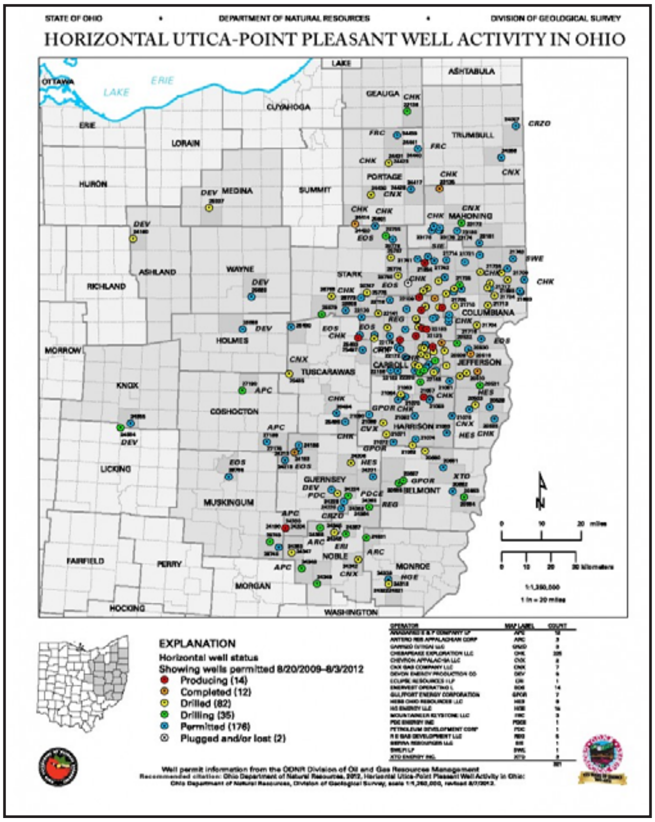
> *Such moves could be a boon for cash-strapped local governments desperate for new revenue…but will also create new risks and potential conflicts as these governments attempt to both maximize their financial returns, while at the same time safeguarding the public interest and infrastructure*

Continued influx of oil and gas support services companies will drive near-term commercial property and construction demand.

The stock of existing industrial facilities in and around the major shale areas has already been snapped up, according to local property brokers, and the director of business development at the Carroll County Chamber of Commerce. The vice president in industrial and corporate real estate at Ostendorf-Morris believes that the influx of the "supporting cast" will continue to drive the market, noting that these companies differ from the general manufacturing sector because they know where they want to be, and they don't haggle over the price.

> *The trend should continue as long as there is new demand for these services from an expanding exploration and production sector. We expect such demand to be strongest in those areas of new exploration and*

permitting (green and blue pins on example Utica map, inset), as well as adjacent to strategic transportation and transshipment hubs. However, it's too early in the shale growth cycle to predict how deep -- or long lasting -- the cycle will be (see also "Shale as a driver of the national economy," below).



The future of commercial transportation: Development of a natural gas transportation - fueling infrastructure.

Shell Oil and TravelCenters of America recently announced an agreement to build 200 natural gas lanes at 100 or more TravelCenter stations along US highways.

Shell and TravelCenters are betting that the demand for such services will emerge --perhaps only after a critical mass of infrastructure has been built. Separately, T. Boone Pickens, Chair of the hedge fund BP Capital Management, has been lobbying for several years in support of his "Pickens Plan" to promote domestically produced natural gas as a major transportation fuel.

Next wave of development likely to include plastics and chemicals manufacturers.

Jacob Duritsky, Director of Business Attraction for the non-profit economic development organization Team NEO, believes the increased production of wet gas, which contains butane and ethane, will attract plastic and chemical manufacturers and drive future commercial property demand in the region. Shell Oil is reportedly considering a site in Beaver County, PA for the construction of a $4 billion ethane "cracker" refinery, which would produce chemicals to make a range of plastic products. One plastic toy company in Ohio, Step2, has already announced a major expansion for its two plants to increase capacity for manufacturing toys, household items and new products it plans to introduce. The expansion will create 200 jobs in the areas and was encouraged by tax incentives and the proximity to natural gas producers, from which the company derives materials.

Neighboring Pennsylvania is actively seeking to promote this type of next-phase development by offering large tax incentives in the hope of luring Shell's proposed ethane cracker facility. If such a facility is built in the region, it can be expected to catalyze spinoff development in the surrounding area.

Realization of indirect and induced economic benefits.

Other industries in the Utica and Marcellus region are receiving a boost from the growing oil and gas sector, and this is evident in general commercial property data. Statewide commercial property delinquency rates have dropped from 11.3% to 8.7% within the past year. Looking at specific industries, hotel occupancy rates are up significantly, and demand for restaurant/food services is increasing. This activity is driving (or at least supporting) new construction and real estate activity -- for example, Cafaro is building a new 103-bed Residence Inn by Marriott in Niles. Quantifying the full impact of the shale boom is difficult, and competing estimates -- from a high of 204,000 new jobs created by 2015, to a low of just 20,000 new jobs over the same timeframe -- have recently been published and debated in the media.

Economic benefits from the shale oil and gas boom can be categorized in three forms: direct -- the investments, local returns, and increased employment created by the oil and gas industry; indirect -- those benefits created due to increased demand on local suppliers for the industry; and induced -- benefits springing from the increased spending of businesses and local employees of companies in the oil and gas sector and their suppliers. Calculating these benefits is an inexact science, and is prone to bias and controversy. It is clear, however, that sustained oil and gas activity in northeast Ohio can increase business in other elements of the economy, driving -- at some level -- demand for commercial and industrial real estate and construction.

OHIO REAL ESTATE AND CONSTRUCTION PROJECTS MAKING NEWS

Company	Business	Location	Size/Cost/Scope
Mc Junkin Red Man Corp (aka MRC Global)	Pipes and valves distributor	Carroll County	330 acres, new warehouse construction
Chesapeake Energy Corp	Natural gas supplier	Ohio-wide	1.35 million acres of leases, $2 billion (though is in process of selling 337,000 acres of “non-core” Utica shale leases
Chesapeake Energy Corp	Natural gas supplier	St. Clairsville	Offices on 30 acres at Fox Commerce Park, land purchased for $300,000
Chesapeake Energy Corp	Natural gas supplier	Harrison and Columbiana Counties	In partnership with **M3 Midstream** and **EV Energy Partners**, plans to build $900 million worth of natural gas gathering and compression facilities
Vallourec SA	Steel tube production	Youngstown	New mill, new construction, $650 million
Weatherford International Ltd	Oilfield services	Youngstown	153,000+ sqf building on 20 acres, $3.4 million
BP Plc	Oil and gas supplier	Trumbull County	Field office and 84,000 acres of leases

Beusa Energy/Beland Energy Utica LLC	Natural gas supplier	Ohio - TBD	Seeking 15-20,000 acres in initial leases
Closed Loop Refining & Recovery	Refiner	Columbus	289,000+ sqf leased industrial facility
FirstEnergy Corp	Power Supplier	Toronto	Selling remediated 60 acre site on Ohio River (former power plant), rumored asking price = $200,000/acre
Baker Hughes Inc	Oilfield Services	Massillon	Plans to build $40 million service center and office building on 100 acres
Exterran Holdings Inc	Oilfield Services	Youngstown	Building a 65,000 sqf factory

NATIONAL TRENDS AND NEWS

Shale as a driver of the national economy, as well as the real estate and construction sectors.

Nationally, the shale gas industry is expected to add $188 billion to the US GDP and support 870,000 jobs by 2015, according to a report by IHS Global Insights (sponsored by America's Natural Gas Alliance). IHS and advocates such as T. Boone Pickens also predict that an expanding domestic natural gas production industry will lower energy and transportation costs, giving an additional boost to the national economy.

On the real estate front, analysis from the CoStar Group from earlier this year predicts a general upswing in the industrial market due to growth in shale production, as well as a small rebound in domestic manufacturing. And CBRE reports that nationally, sales of industrial properties hit a record high of $2.5 billion in Q2 2012—led by a single, multi-property deal worth $770 million). In addition, CBRE found declining industrial vacancy rates and increasing rents.

And, while a June report by the Associated General Contractors of America found construction jobs dropping in half of the 337 metropolitan areas surveyed, the picture in the Marcellus-Utica shale region showed modest growth, including +4% for Ohio.

> *We find a broad set of indicators pointing toward continued growth in the industrial real estate and construction sector, driven by the shale gas boom. However, we are still early in the "upswing" of this cycle, and it remains to be seen how deep—and lasting—this trend will be. Some analysts, for example London's Financial Times, caution that even at the levels predicted by the IHS Global Insights report, growth in the shale gas sector alone will not be enough to drive significant growth in the overall economy.*
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> *Finally, while shale-related activity is on an upswing, we note that both nationally and within Ohio, real estate and construction activity related to the US Governments fiscal stimulus efforts is declining, and will continue to do so for the foreseeable future*

Additional Information

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