

# REVERSING THE TIDE

Strategies for Successful Rural Revitalization

## Case Study

### Kentucky Highlands Investment Corporation (Kentucky)



Written in the fall of 2008

This case study has been produced as part of the 'REVERSING THE TIDE: Strategies for Success Rural Revitalization' project. The purpose of this case study, along with three others, is to provide insight into the goals, structures, and investment/ program strategies that well respected, successful organizations concerned with rural regional revitalization have used to address economic and community issues in rural areas.

# Kentucky Highlands Investment Corporation (Kentucky)

Note to Reader: This paper is a compilation of written material taken directly from documents on the KHIC website and from a March 2003 Research Case Study Paper prepared by the Centre for Rural Entrepreneurship titled “Development of an Entrepreneurial Support Organization: The Case of the Kentucky Highlands Investment Corporation” by Deborah Markley and David Barkley; Center for Rural Entrepreneurship.

***The Kentucky Highlands Investment Corporation’s (KHIC) four-decade long track record of success in the community development venture capital (CDVC) line of business has demonstrated that it is possible to profit from investments that promote job and wealth creation in poverty-stricken regions such as Southern Appalachia. KHIC has helped to create or retain more than 10,300 jobs by investing approximately \$165M in over 500 businesses. KHIC has been a vibrant catalyst for change in its target area. Its investment portfolio companies produce goods and services valued at \$13.5B; pay more than \$1.9B in salaries and wages; and generate an estimated \$300M in tax revenue.***

Click on [www.khic.org](http://www.khic.org) to access their website.

## **KHIC’s SERVICE AREA**

Originally, the Kentucky Highlands Investment Corporation (KHIC) was created to serve a nine county geographic area in Appalachian southeastern Kentucky. In 2003, this service area was increased to serve a 22 county area in the same part of the state. This 22 county area has a population of approximately 500,000. KHIC’s service area is definitely rural – there are only four population centers in the service area that have a population of over 5,000 residents. The main thrust of KHIC’s activities throughout its long history has been to create jobs within their service area.

Figure 1 on the following page shows a Map of KHIC’s service area. In 2003, KHIC expanded the service area to 22 counties: Bell, Clay, Clinton, Cumberland, Estill, Harlan, Jackson, Knox, Laurel, Lee, Leslie, Letcher, Lincoln, Madison, McCreary, Owsley, Perry, Pulaski, Rockcastle, Russell, Wayne and Whitley.

## **HISTORY OF THE KENTUCKY HIGHLANDS INVESTMENT CORPORATION**

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**Kentucky Highlands was built on the basic premise that significant reduction in poverty in the area could not be achieved without economic growth.**

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In the 1960’s, the economy in southern Kentucky was in severe trouble. The once solid industries of mining, agriculture, textiles and wood products were in severe decline and there were few organizations in the region promoting local economic development. As a result, in 1968 six Kentucky community action agencies collaborated to apply to the US Federal Government’s Office of Economic Opportunity (OEO) to become a Title VII Community Development Corporation. Their submission was approved and under the name Job Start Corporation, the foundation for what has become KHIC was built. Job Start, with core funding from the Office of Economic Opportunity, was charged with stimulating community and economic development in a nine-county region of south eastern Kentucky. At this time, employment opportunities in the area were dominated by declining industries (mining, agriculture, textiles, and wood products), and the region was experiencing poverty and unemployment rates that were significantly above national averages. In response to this situation, the adopted mission of Job Start was “to provide and retain employment opportunities in south eastern Kentucky through sound investments and management assistance.” In the early years, Kentucky Highlands had to address a number of local problems outside the immediate realm of business development. They engaged in anti-poverty and housing programs, community development, training for community organizations and the development of industrial parks. They also recruited businesses to come to the area and funded entrepreneurial development projects. From 1968 to 1980, KHIC received approximately \$14M from various sources to support operations and investments in areas businesses. Early efforts included KHIC directly starting and managing businesses, but this method was dropped due to lack of staff and resources. In 1980 President Reagan ceased funding for the OEO, which eliminated KHIC’s principal source of grant funding.

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**In 1972 KHIC tested a new technique that would locate aspiring entrepreneurs, choose the most promising and then finance their new business as long as it was located in one of the target communities and promised to hire unemployed**

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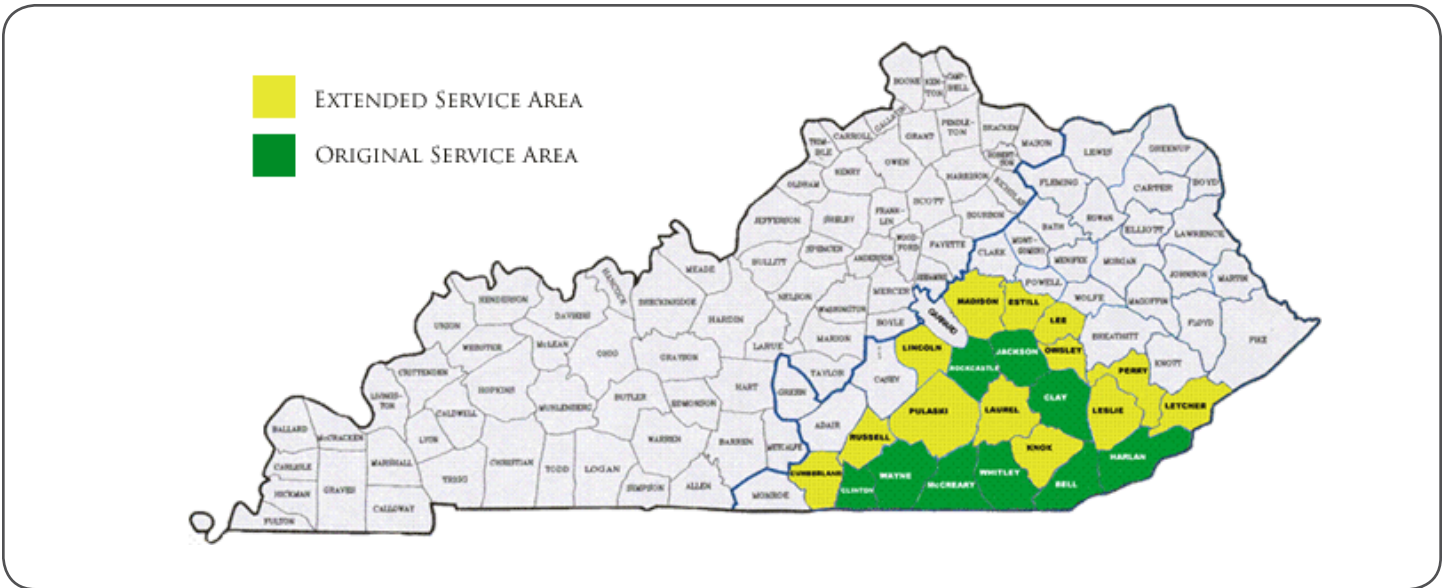


Figure 1: Kentucky Highlands Service Area. © Kentucky Highlands Investment Corporation.

**residents. In return for offering hard-to-locate start up capital and fair financing terms, KHIC would take ownership positions. KHIC did not offer low rate financing. If a business was viable, it could afford to pay for its risk capital. This process became known as “development venture capital.” Development venture capital investing involves more active participation with management of the businesses than does traditional venture capital investing.**

The loss of grant funding opportunities in 1980 coincided with a change in KHIC leadership and a shift in program emphasis from creating jobs to supporting entrepreneurs who could create new companies. KHIC economic development efforts in the 1980s became increasingly focused on stimulating business development. KHIC worked closely with entrepreneurs to develop their business plans and when appropriate provided venture and debt capital to support the new firms. KHIC personnel were also very active in assisting or managing struggling companies that were part of their investment portfolio. KHIC found that their clients required more technical support than portfolio companies of traditional venture capital funds. Entrepreneurial skills were scarce among the indigenous population and new companies faced a business environment lacking in support services and infrastructure.

In 1989, leadership of KHIC changed again and the new CEO emphasized finding and using new sources of government and foundation funding to support the mission of creating and nurturing companies. In the next 10 years KHIC increased the diversity of its financial offerings with the addition of a number of federally funded programs including the United States Department of Agriculture (USDA) Intermediary Relending Program; US Small Business Administration Micro Loan Program; USDA Business and Industry Guaranteed Loan Program; Empowerment Zone Venture Capital Fund; New

Markets Venture Fund; and the Community Development Financial Institutions fund. In addition, Kentucky Highlands received funds from a number of sources for revolving loan funds (USDA’s Rural Business Enterprise Grant program, Office of Community Services, US Department of Housing and Urban Development, and the Appalachian Regional Commission). Program related investments from the Ford Foundation and the MacArthur Foundation were also used for revolving loan funds and equity investments. KHIC also borrowed funds from the Rural Local Initiative Support Corporation for relending to companies in the region. Current KHIC activities are balanced between development venture capital activities (finding, starting, and supporting new business development) and increasing the breadth of program offerings for area businesses through aggressive grantsmanship.

Table 1 on the following page provides a timeline of KHIC’s organizational evolution to date.

As Table 1 indicates, KHIC did not begin with a complete package of capital tools but rather evolved this toolkit over time. The organization has been opportunistic in taking advantage of public and private funding opportunities to expand the amount and type of capital that KHIC has access to.

**KHIC TODAY**

**“We invest in some counties where otherwise there would be no investment. Our loyalty and our longevity are what make us unique.”**

*Brenda McDaniel, KHIC Vice-President*

**Table 1: Kentucky Highlands Investment Corporation Timeline**

1968	Founded as Job Start Corporation
1971	Possum Trot established as first manufacturing operation
1972	Kentucky Highlands begins making venture capital investments with its first investment in Outdoor Venture Corporation
1980	Small Business Administration awards Kentucky Highlands a Small Business Investment Corporation (SBIC) license for Mountain Ventures, Inc.
1980	Kentucky Highlands makes equity investment in Mount Vernon Plastics
1991	Kentucky Highlands named 1 <sup>st</sup> Intermediary Relending Program participant in Kentucky by the U.S. Department of Agriculture
1992	Kentucky Highlands approved as first U.S. Small Business Administration Microloan lender in Kentucky
1994	Kentucky Highlands becomes founding member of Community Development Venture Capital Alliance, a national and international organization. KHIC also successfully exits Mount Vernon Plastics and American Bag Company
1994	Kentucky Highlands named among the first Tax Credit Community Development Corporations in the country by the U.S. Department of Housing & Urban Development
1994	Kentucky Highlands Empowerment Zone named as one of only three rural zones in the United States
1995	Kentucky Highlands becomes founding community development partner for Rural Local Initiative Support Corporation
1996	Kentucky Highlands named first-round Certified Development Financial Institution (CDFI) by the U.S. Department of Treasury
1997	Kentucky Highlands named the first non-bank lender in the nation by the U.S. Department of Agriculture Business & Industry Guarantee Loan Program
2002	Kentucky Highlands forms the Appalachian Development Alliance in partnership with six regional lenders
2003	Kentucky Highlands expands its service area to 22 counties
2003	Kentucky Highlands partnership company, Southern Appalachian Fund, named as one of only six New Market Capital Companies by U.S. Small Business Administration
2005	Kentucky Highlands receives \$22 million allocation through the New Markets Tax Credit program by the U.S. Department of Treasury
2006	Kentucky Highlands partnership company, Meritus Ventures, approved as the only Rural Business Investment Company in the nation by U.S. Small Business Administration and the U.S. Department of Agriculture

The main mission of KHIC has remained unchanged since Job Start was founded in 1968; however, the region has evolved in that residents and businesses are less isolated, education and training opportunities are more easily accessible, and economic and community development organizations are more prevalent and sophisticated. Development within the service area has permitted KHIC to focus program offerings on financial and technical assistance for area entrepreneurs and small businesses.

KHIC currently deploys a range of investment instruments that help start-up and expanding companies provide jobs to chronically poverty-stricken Appalachian east Kentucky, including equity investment, subordinated debt, term loans for real estate and equipment, revolving lines of credit, and micro loans. In addition to financial support, KHIC supplies business assistance that most entrepreneurs could neither obtain nor afford. KHIC provides management assistance in the areas of finance, systems analysis, personnel recruitment, training, accounting, cash management, and financial restructuring. KHIC's staff also has skills in negotiation with both secured and unsecured creditors and local governments and offers management assistance in troubled situations, as well as technical support to troubled IT projects. This level of support is vital to smaller enterprises in rural Appalachia, where low population densities often make enterprise operations more costly and negatively affect productivity. These challenges create disadvantages for struggling entrepreneurs as they try to attract workers with skills important to today's knowledge-based economy.

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**Like most of rural America, Appalachia is not an area to which large venture capital firms are typically drawn. Currently less than one percent of private equity raised through venture capital firms is invested in rural markets.**

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KHIC tailors its operational assistance to meet the specific needs of each individual company, which may include activities such as investing in the preparation of business plans, development of marketing strategies, creation of Internet and Web site capabilities, supporting the establishment of accounting systems, providing technical assistance to optimize a production process, management recruitment, and legal advice on preservation of intellectual property. KHIC can provide some of the services directly to the companies and contract with appropriate professionals to provide these services when they are not qualified to do so.

## **MAJOR OPERATIONAL ACTIVITIES OF KHIC**

The majority of KHIC's current day to day operational activities occur in six major fields of work: entrepreneurial development; providing technical business support; providing and managing a loan portfolio; providing and managing venture capital funds; industrial development support; management of a federally funded Empowerment Zone; and other community and economic development initiatives.

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**"However, most entrepreneurs do not bring a full set of skills to the process of enterprise creation, thus their success is dependent on their ability to access support services within the local market. For entrepreneurs operating in rural markets, the limited support service infrastructure creates a significant obstacle to business creation and growth. The development of an entrepreneurial support infrastructure in rural regions is an important strategy for encouraging entrepreneurship and rural economic development."**

*Markley & Barkley, March 2003*

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## **Entrepreneurial Development**

KHIC continues to support and manage a series of initiatives to encourage entrepreneurial development, including entrepreneurial training courses, delivering an 'energy bootcamp' training program and operating a business incubator at KHIC's head office. The KHIC Energy Boot Camp is an intensive performance-based Entrepreneurial training and mentoring program conducted in partnership with Technology 2020's Center for Entrepreneurial Growth (CEG) in Oak Ridge, Tennessee. The purpose of the boot camp is to help energy-related researchers, inventors, and entrepreneurs prepare a path to business sustainability and profitability. Located at KHIC's offices, the six-month long program features (4) four-hour entrepreneurial management development training classes with homework assignments; individualized coaching sessions specific to the needs of the client company; (2) energy-focused evening network events to help generate opportunities, meet potential partners and strategic area resources; and participation in a regional Energy Symposium at the end of class.

In 2006, KHIC established a small business incubator—the Center for Entrepreneurial Growth—at its London, KY headquarters. The incubator has enough room to house three companies and focuses on technology businesses or those that leverage technology in their business model. There are three main benefits to a business locating in the incubator—business owners participate in a formal entrepreneurial management development training program and receive coaching and mentoring from experienced entrepreneurs; and entrepreneurs have access to capital if their businesses meet milestones and accomplishments identified in their business plans.

## **Providing Small Business Technical Assistance and Support**

Part of what distinguishes a capital-led economic development program, like Kentucky Highlands, from more traditional venture capital funds is the provision of hands-on, customized technical assistance to entrepreneurs. Particularly in the south eastern Kentucky region, entrepreneurs often lack the business and



technical skills necessary to manage a successful business enterprise. The KHIC model recognizes these potential limitations and works with the entrepreneurs to develop the requisite management capacity. KHIC provides three principal types of technical and managerial assistance to local entrepreneurs and businesses. First, KHIC works one-on-one with a business after the company becomes a member of the KHIC portfolio. Technical assistance provided by KHIC includes devising strategies and business plans, developing markets and marketing products, developing treasury skills in terms of managing flow of funds for collections and payables, getting good terms of credit with suppliers and creditors, and getting access to credit from local banks. KHIC will also provide these services for an entrepreneurial team but a fee will be charged for the assistance if the entrepreneurs go elsewhere for funding. Second, KHIC may take over management of a portfolio company if the firm defaults on its equity or loan agreement. KHIC also may undertake a “constructive takeover” whereby Kentucky Highlands stipulates that future loans or equity investments will be forthcoming only if the business meets certain conditions. Third, Kentucky Highlands has offered technical assistance to entrepreneurs and small businesses through its business-planning center (The Launching Pad). The Launching Pad is an Entrepreneurship Institution funded by the Appalachian Regional Commission, United States Department of Agriculture, and US Small Business Administration and it is the predecessor of the expanded Centre for Entrepreneurial Growth.

## Loan Programs

KHIC offers a variety of loan programs that are each tailored to the size and needs of local small businesses:

**MICRO-ENTERPRISE LOAN FUND:** This fund was established to serve very small businesses with loans of up to \$35,000. Loans are offered at fixed rates for a maximum of 72 months. Loans can be used for either working capital or equipment.

**SMALL BUSINESS LOAN FUND:** This fund provides loans up to \$250,000 to small businesses at a fixed rate for periods of 5–15 years. Business expansions and start-ups are supported through this program. Working capital, equipment and real estate are all eligible uses for the loan.

**WORKING CAPITAL OR LINES OF CREDIT:** These specific needs are typically met through loans of one year. A portion of these loans are sometimes sold to banks. Turning Point Capital Fund is the vehicle for some of the working capital needs. Part of Turning Point’s capitalization came from a grant from the US Department of Housing and Urban Development’s (HUD) Rural Housing and Economic Development program. Other funds came from a 2.75% loan from the Federal Home Loan Bank of Cincinnati.

**BUSINESS AND INDUSTRY LOAN GUARANTEES:** KHIC has been designated as a guaranteed lender through the Department of Agriculture’s Business and Industry Loan Guarantee Program.

This program allows KHIC to make loans up to \$10M and receive a guarantee from USDA. This enables KHIC to offer long term fixed rate financing.

**APPALACHIAN DEVELOPMENT ALLIANCE:** KHIC joined with seven other groups serving Appalachian Kentucky to establish a lending collaborative, the Appalachian Development Alliance. Together, the Alliance is able to get more resources from the state and the private sector than any one of them could do alone. They can reach 700,000 people and together have \$120M available for deals.

## Venture Capital Funds

One of KHIC’s main tools for creating jobs is through direct equity investment by KHIC (and its subsidiaries) in small businesses. This offers the possibility of a larger financial return to KHIC, but also carries with it a larger risk:

**SOUTHERN APPALACHIAN FUND:** KHIC is the managing partner in the \$12.5M venture capital fund—the Southern Appalachian Fund—which covers Kentucky, Tennessee, and the Appalachian counties of Georgia, Alabama, and Mississippi. The fund was capitalized through the federal US New Markets Tax Credit Program; its partners include Bank One, Concord EFS, Farmers & Merchants, First Bank, National City Bank, and Tennessee Commerce Bank.

**OTHER VENTURE CAPITAL FUNDS:** KHIC manages approximately \$40M in two other venture capital funds (Meritus Ventures and Mountain Ventures) that are used for investment in local businesses. Meritus Ventures is the only Rural Business Investment Corporation and Mountain Ventures is a Small Business Investment Corporation both licensed by the US Small Business Administration.

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***KHIC pioneered development venture capital investing, which involves more active participation in business management than typically involved in traditional capital investing.***

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## Industrial Development

KHIC’s strategy for industrial development is to invest in prepared sites that facilitate rapid construction of light industrial facilities. Through a program called LEAP (Land, Excavation, Architectural and Piers) sites are completely prepared to immediately begin the erection of up to a sixty thousand square foot building. These sites are then sold to companies wanting to expedite construction. KHIC has also constructed, financed and leased buildings to qualified clients.

## Management of a Federal Empowerment Zone

In a unique approach, KHIC applied and was designated as the lead organization for a rural Empowerment Zone through the United States Department of Agriculture's Rural program. KHIC was only one of three Empowerment Zones (EZ) approved in the US and covers Clinton, Jackson and Wayne counties. The EZ designation was made in December 1994 and included a grant award of \$40M. Before 1994, the 30,000 people living in the isolated communities of these three counties had difficulty obtaining basic services such as tax assistance, dry cleaning, and medical services. The three-county region faced huge economic development obstacles. Important economic indicators were much worse than state and national averages—an unemployment rate of 9.3%, a poverty rate of 38%, and average annual wage of \$15,000, a per capita annual personal income of less than \$12,000 and a population where less than 43% of those age 25 years and older had a high school diploma or GED.

## Other Community and Economic Development Initiatives

The efforts of KHIC are not limited to business development. Kentucky Highlands Investment Corporation recognizes the importance of lateral development if a region is to prosper. They have been partners in numerous community development projects, including a residential home for disadvantaged youth, establishment of a sheltered workshop, providing housing assistance for families in need, and the financing of youth centers, libraries and theaters for area residents. KHIC is also active in a collaboration between the States of Kentucky and Tennessee to recruit a bio-defense lab to Pulaski County. The collaborative effort to compete for a \$500M national bio-defense lab is being led by the two governors, four U.S. senators, three universities (University of Kentucky, University of Louisville and University of Tennessee), KHIC, the Center for Rural Development, the Oak Ridge National Laboratory, the National Institute for Hometown Security and the Southeast Kentucky Economic Development Corporation. If successful in being selected, the facility would have created more than 400 permanent jobs with an average salary of \$74,000 and a payroll of \$30M. Another cooperative effort with Tennessee is the Tennessee Valley Corridor, which is a non-profit organization dedicated to promoting the Tennessee Valley Corridor as one of the nation's premier science and technology centers. It also seeks to leverage the corridor's world-class research institutions and technology assets for maximum regional economic development and new job creation. Finally, KHIC has recently received permission to obtain up to \$32M in New Markets Tax Credits from the CDFI Fund, US Department of Treasury, to attract investments in its service area.

## KHIC's ORGANIZATIONAL STRUCTURE

KHIC is currently governed by a seventeen member Board of Directors. The board has a wide variety of backgrounds including

people with experience in business, banking, farming, education, local government, law, public administration, medicine, human services, agricultural development, arts and tourism. They are representative of the area's diversity of geography, income levels, and vocational interests.

KHIC currently has a staff complement of 18 in the following positions:

- President & Chief Executive Officer
- Executive Vice President & Chief Operating Officer
- Executive Vice President & Chief Financial Officer
- Vice President of Housing
- Vice President of Business Lending
- Investment Analysts (2 positions)
- Business Development Specialist
- Technical Systems Engineer & Investment Analyst
- Development Director
- Special Projects Coordinator
- Senior Accountant/Controller
- Accountants (4 positions)
- Executive Assistant
- Administrative Assistants (2 positions)

To administer the variety of loan and venture capital funds that KHIC manages, KHIC has several subsidiary companies and collaborative partnerships as described below:

**Southern Appalachian Fund (SAF) (2001)** is a \$12.5M venture capital fund formed to provide equity capital and operational assistance to qualifying businesses in southern Appalachia. The Fund is the result of collaboration between KHIC and Technology 2020 of Oak Ridge, Tenn. The Southern Appalachian Fund is one of six New Markets Venture Capital (NMVC) Companies in the United States. The NMVC Program is a developmental venture capital program designed to promote economic development and the creation of wealth and job opportunities in low-income geographic areas and among individuals living in such areas. Participating individuals, banks and other financial institutions receive credit against federal income taxes for making qualified equity investments in NMVC community development entities, like KHIC. The Southern Appalachian fund is capitalized with \$12.5M, \$5M raised from institutions concerned with economic

development in Appalachia (e.g., Appalachian Regional Commission, Tennessee Valley Authority, two private foundations and several banks in Tennessee, Kentucky and Ohio) and \$7.5M in federal matching funds (1.5 to 1 match). Investments by SAF are limited to low-income census tracts (80% of state median income, 20% in poverty) in Kentucky, Tennessee, N. Georgia, N. Alabama, and N.E. Mississippi. The Fund's mission is to generate market-rate returns for its investors while promoting shared and sustainable business growth and wealth creation throughout its target region. The Fund was set-up to invest in companies with strong management teams, high growth potential, and defensible market positions. The Fund Managers also work to add value to the Fund's portfolio companies through operational assistance, active board participation, and mentoring. SAF will be operated as a limited partnership with a 10-year life. KHIC and Technology 2020 are the general partners, and they will receive 25% of the earned interest. Other investors in the fund (the limited partners) will receive the principle plus 75% of earned interest. The Fund is now fully invested in eight start-up and expansion stage companies that include manufacturing, software and technology.

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**Entrepreneurs in south eastern Kentucky face additional challenges because more than 80% of venture capital is invested on the East or West Coast, and technical assistance providers outside of large metropolitan areas are often limited or cost prohibitive. That means the two essential components for a successful start-up company are often more elusive, particularly in a state such as Kentucky.**

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The **Meritus Ventures Limited Partnership (Meritus)** is a collaboration between KHIC and Technology 2020. It serves a larger portion of Appalachia and focuses on companies that are expanding. Meritus Ventures, licensed in 2006 by the US Small Business Administration and the US Department of Agriculture, is the only Rural Business Investment Corporation in the US. It began with \$12M from 22 initial investors and grew to \$36.4M through the sale of USDA guaranteed debentures. The Fund's mission is to generate market-rate returns for its investors while promoting shared and sustainable business growth and wealth creation throughout its target region. The Fund will invest \$250,000 - \$2,500,000 in companies with strong management teams, high growth potential, and defensible competitive advantages. The Fund focuses on manufacturing, technology and software businesses. The Fund Managers also add value to the Fund's portfolio companies through operational assistance, active board participation, and mentoring.

The **Mountain Ventures Inc. Small Business Investment Corp. (SBIC)** is a \$7.5M dollar fund (including 300% leverage) that provides both debt and equity financing. Funds from Mountain Ventures SBIC are the only KHIC program monies that may be co-invested with equity investments from the original

KHIC Fund, and all profits (earned interest) from the deals are used to capitalize the KHIC and Mountain Venture Funds.

The **USDA Intermediary Relending Program (IRP)** provides a way to meet the needs of entrepreneurs who can not qualify for bank financing. Entrepreneurs come to KHIC when they cannot get a loan elsewhere in the region. Under the USDA IRP, the USDA makes a direct loan to KHIC at an annual interest rate of 1% for a maximum of 30 years. KHIC then makes loans from this revolving fund to businesses in the service area that do not qualify for bank financing. Maximum deal size is \$150,000 with the exception that 25% of the deals may be up to \$250,000. All loans to area companies are made at slightly less than market rates and are secured by collateral. KHIC submits each potential deal with a portfolio company to USDA and the Kentucky State Environment Clearinghouse for approval. All repayments on the IRP loans are kept by KHIC except for the amount required for annual loan payments to USDA. The remaining interest income and fees may be used for KHIC administrative costs, technical assistance, and fund replenishment. The IRP Loan Fund has made approximately 35 loans to area businesses and has used about \$4M of the \$15M allowed by USDA program guidelines.

The **Kentucky Highlands Empowerment Zone Development Venture Capital Fund (KHEZ)** was capitalized with \$12M; with \$11M targeted for general business and \$1M for agricultural activities. In addition, \$2M of EZ funding was used to capitalize the Mountain Venture SBIC, but loans based on the capitalization can be made only in the three EZ counties (Clinton, Jackson, and Wayne). The loan focus for the KHEZ Fund is manufacturing and specific professional services. Loans are primarily long term, fully collateralized, with fixed rates of interest. A separate loan committee was established to approve KHEZ loans, and for the first seven years of the program, KHEZ investments could not be made in a company that also received financial assistance from another KHIC program. However, profits and interest earned on the KHEZ fund's investments remain in the KHIC Venture Fund, and KHIC is reimbursed for project management out of the EZ general budget.

In the late 1990s, Kentucky Highlands added another federal program, the **Nonbank USDA Business and Industrial (B&I) Lender (1997)**, to its capital toolkit. KHIC became a B&I lender to provide an additional source of funds for area businesses and to assist area banks by packaging these loans. The B&I program permits KHIC to make larger deals (minimum of \$250,000 up to \$10M for special cases) than other lending programs available to them. The USDA B&I Guaranteed Loan Program provides guarantees (80%, 90% within the EZ) for loans made by eligible commercial lenders to rural businesses. Loan proceeds may be used for working capital, equipment, and real estate. Currently, KHIC has participated in \$12M of B&I loans, 7 loans originated by KHIC (4 closed, 3 in progress) plus other loans in partnership with area banks.



The **Appalachian Development Alliance (2002)** is a consortium of nine area economic development organizations (Pine Mountain Development Corporation, Southern Kentucky Economic Development Corporation, East Kentucky Corporation, Mountain Association for Community Economic Development, Mountain Economic Development Fund, HEAD Loan Fund, Community Ventures, Jackson County Entrepreneur Center, and KHIC). The Alliance allows these organizations to collaborate and tap into funds that might not otherwise be available, such as state funds. ADA operates as a fund of funds, with each organization providing capital (minimum of \$50,000) and different areas of expertise and specialization. The Alliance serves a broader geographic area than the 22 counties in KHIC's service region, and the larger geographic region makes ADA eligible for state assistance. ADA recently received \$1M from the Kentucky coal severance tax fund, and the Alliance has also received CDFI funding. It is planned that each of the organizations in ADA may borrow from the Alliance after it receives external funding.

**SCALE OF KHIC'S RESOURCES AND PROGRAM EXPENDITURES**

In a typical year, KHIC will make 50 to 90 loans worth \$8 to \$16M and another 5 to 10 equity investments worth another \$500,000 to \$2M using KHIC's own organizational funds. Each dollar directly invested by KHIC into a business will typically lever an additional \$2 to \$3 in financing from other financiers for the business venture.

As of March 31, 2008 KHIC had 322 active loans and equity investments in their portfolio worth an estimated \$35M.

KHIC's annual administration costs are approximately \$4,000,000 per year. These administration costs are covered primarily by KHIC interest and equity earnings, management fees from the investment funds and from other fee for service revenue. Table 2 provides a summary description of KHIC's annual revenue and investments.

**EXAMPLES OF KHIC'S INVESTMENTS & PROJECTS**

The Kentucky Highlands **Energy Business Boot Camp** is an intensive performance based entrepreneurial training and mentoring program that is being conducted in partnership with the Center for Entrepreneurial Growth, which has offices in Oak Ridge, Tenn., and London, Ky. The boot camp focuses on helping energy-related researchers, inventors and entrepreneurs create a fundable, sustainable and profitable business model that will help create jobs in the region. Five entrepreneurs were selected for the first boot camp in 2008. They participated in intense training sessions, received individualized coaching and received assistance in developing a business and funding plan. The five diverse entrepreneurial teams are developing fundable and sustainable businesses based on the following:

**Table 2: KHIC Summary of Annual Revenue and Expenditures**

<b>Cash in and Revenue:</b>	
Interest Earnings from Loans/Rental Income/and Earnings/Returns from Equity Investments	\$5.2M
Management Fees from Portfolio/Fund Management	\$1.2M
Grants from Foundations/Government	\$2.3M
Principal Repayments	\$8.0M
<b>Total Revenue</b>	<b>\$16.7M</b>
<b>Expenditures:</b>	
Loans	\$9.8M
Equity Investments	\$1.0M*
KHIC Administration Costs	\$4.2M
<b>Total Expenditures</b>	<b>\$15.0M</b>

\*An additional \$53M in equity investments were made using funds from KHIC affiliated venture capital funds or from venture capital funds where KHIC is a financial partner or the general managers of the fund:

- \$16.5M by KHIC New Market Tax Credit
- \$14.5M by KHIC
- \$9.4M by Meritus Ventures
- \$12.7M by Southern Appalachian Fund

- Wind farms on reclaimed Eastern Kentucky ridge-top coal mines;
- Manufacturer of biodegradable 100 percent loss lubricants and greases;
- The use of fly ash in both plastic and metal alloys to enhance physical properties;
- The conversion of biomass products to syngas; and
- A company using thermobaric energy processes and systems to produce new energy and deal with serious environmental issues.

It is expected that these companies will become major contributors to economic impact and the growth of new technologies in Eastern Kentucky. In turn, those businesses will impact the entire region by employing people, creating profits and helping solve the nation's growing energy problems.

**Tri-County Manufacturing and Assembly, Inc. (TCA)** is a company that has seen its share of ups and downs. The company, located in Williamsburg, Kentucky, was primarily a contract manufacturer of printed circuit board assemblies. After surviving a very difficult period in 2002, it seemed that TCA was on the upswing when its original owners returned to manage the company. The company fared well

for a while, but faced new and difficult challenges in 2003 that nearly brought the company's demise. With almost 200 manufacturing jobs at stake, Kentucky Highlands sent staff members Elmer Parlier and Melissa Conn to work on-site at TCA to stabilize the company until new owners could be found. In January 2004, electronics manufacturer CDR Manufacturing purchased the assets of TCA and began operating the plant as its own.

With the right support, the companies capitalized by the Southern Appalachian Fund not only grow, they thrive. One such firm, **Tricycle, Inc., Chattanooga, Tennessee**, earned a 2006 Excellence Award from the Community Development Venture Capital Alliance for its innovative human initiatives; creation of sustainable, quality jobs; significant progress toward its financial goals; performance in the marketplace; and outstanding management capacity. Tricycle's business is both unique and specialized. The company serves the commercial carpet industry, in particular the high-end market for carpets designed by decorators and interior designers. The innovation Tricycle brought to this industry was the use of technology to create a paper carpet sample that mimics the color and texture of an actual carpet sample, which replaced the then-current practice of having carpet manufacturers make actual samples of the interior floor coverings drawn by designers. In 2005, Tricycle's digital carpet modeling services helped interior product manufacturers conserve 9,425 gallons of oil, kept 56,500 pounds of carpet out of landfills, and saved more than \$5M.

Another example of KHIC's success is **Cumberland Gap Provision Company, Middlesboro, Kentucky**. Founded in 1979 by Ray McGregor to produce locally cured hams, Cumberland Gap turned to KHIC in 1991 when it needed help developing an employee-owned company. At that time, KHIC also invested equity in Cumberland. In 1996, the company repurchased KHIC's stock, but KHIC continued its involvement in the expansion of the company through a grant from the Office of Community Services to expand Cumberland Gap's operation. In 2003, Smithfield Foods purchased Cumberland Gap. Today, Cumberland makes products under its own label, as well as for a number of nationally recognized brands, and employs 320 people in a facility that has been expanded four times and is now more than 100,000 square feet.

When an investment creates jobs, it is considered a success. Then add high wages, good benefits and the improvement of rural health care, and you've got Kentucky Highlands' investment in **Certacare**. Headquartered in Albany, the company was formed in 2006 to provide home infusion therapy to out-patients and recently released hospital patients in southern Kentucky. Home infusion therapy involves administration of medications such as antibiotics and chemotherapy. It has grown from eight employees less than a year ago to 46 employees today, with benefits that include medical insurance, paid holidays, vacation and sick days. "This is exactly the type of company that KHIC sees as a model investment," states Jerry Rickett, president & CEO of Kentucky Highlands. "The

jobs are high paying and won't move out of state because of the nature of the work and the fact that the owners are natives of the area. We are always excited to foster the entrepreneurial spirit of Kentuckians." Kentucky Highlands Investment Corporation provided the company with loans through the Empowerment Zone and the USDA's Rural Business Enterprise Grant program for equipment, inventory and working capital. The initial plan for Certacare was to provide service in nine counties. However, the company believes there are significant opportunities in the market for home infusion and has developed a business plan to grow to 100 locations in eight states.

## HAS KHIC BEEN SUCCESSFUL?

**"We have been successful in maximizing public and private investment capital in an area of the country that traditional venture capitalists have neglected. But the accomplishments are more than mere numbers. For every achievement, there are many families who have gained economic stability. For every success, a solid tax base is created for important government services. For every accomplishment, there is a region that people look to with pride and live in with hope – an enduring legacy for our children."**

*Jerry Rickett, KHIC President & CEO*

Kentucky Highlands has seen steady growth in its investments and net worth over time. Beginning in 1970 with investments valued at \$5,000, KHIC's investments have now grown to a cumulative total of over \$165M. The organization's net worth has increased as well, growing from about \$12,000 in 1970 to over \$40M in 2007. As shown in Table 3 below, KHIC's impacts and achievements are impressive.

**Table 3: KHIC Summary Statistics**

Loans closed	803
Equity investments made	42
Total amount financed	Over \$165M
Jobs created and retained	10,197
Businesses started or expanded	Over 500

Companies in which KHIC has invested have:

- Produced goods and services valued at \$13.5B
- Paid more than \$1.9B in salaries and wages
- Generated an estimated \$300M in tax revenue

Obtained one of only three rural federal Empowerment Zones in the nation, which:

- Resulted in \$40M in investments
- Created 3,600 new jobs
- Reduced poverty and unemployment in the zone by > 30%

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**Over the last 20 years, KHIC has posted an internal rate of return approaching 20%.**

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KHIC is also a valuable community development partner to the area's regional banks in two ways. First, they offer a direct investment opportunity. Some banks may be reluctant to invest in a Community Development Venture Capital Fund like the one KHIC operates because they believe that returns on socially relevant investments are inherently small or that the minimum investment is too large. In reality, KHIC's minimum investment is \$100,000. And, over the last 20 years, KHIC has posted an internal rate of return approaching 20%. While that's only about half of the return traditional venture capital firms typically aspire to, banks that invest in KHIC may also be eligible for Community Reinvestment Act (CRA) consideration. Another common concern about CDVC funds is that they do not pay any returns for long periods. While KHIC has created a 10-year limited partnership with two, one-year extensions, this structure does not preclude a bank from receiving returns for a dozen years. Each investment KHIC makes in local companies includes an exit strategy, and it is common for KHIC investments to start returning cash within three years, or even earlier. For example, in 2005, SAF invested in Eon Streams, Inc. and exited 14 months later, providing a 260 percent rate of return, and creating a gain that will be passed along to the limited partners when the NMTC compliance period allows. Of course, not all of the companies in which KHIC, SAF, Meritus or Mountain Ventures invests exit that quickly, or provide such significant gains. The second way that KHIC participates with banks occurs later in the business cycle of the companies in which they invest. KHIC finds that institutions that do not participate as direct investors often follow up with hard asset and building equipment financing for the businesses whose growth has been nurtured by KHIC.

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**"While each deal between Kentucky Highlands and an entrepreneur is uniquely structured, a number of common themes can be drawn from their experiences with KHIC. One important theme was that Kentucky Highlands provided these entrepreneurs with much more than capital. All of the entrepreneurs identified technical or business assistance provided by KHIC as part of the financing package and indicated the value of this assistance to the business. One entrepreneur described Kentucky Highlands as being more like a partner than an investor. This entrepreneur also indicated that the company would want KHIC representation on the board even if there were no longer a financial relationship. In another case, an entrepreneur sought KHIC staff expertise to help screen applicants for a management position even though this was not required by Kentucky Highlands. Another entrepreneur described how Kentucky Highlands used contacts within the banking community to pull together a financing package and used connections with community officials to help smooth the way for this new business enterprise. One entrepreneur indicated that his**

**company was looking for more than money. The company wanted investors who understood the business and they got such investors in KHIC."**

*D. Markley & D. Barkley, March*

2003

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Appendix 1 provides more excerpts from the conclusions of the Markley and Barkley Case Study noted above. The Case study methodology included interviewing KHIC clients to determine how they perceived KHIC contributed to their business's success. The interview responses clearly indicate that KHIC's approach of providing both technical and financial assistance is highly valued by their clients:

*"While entrepreneurs benefited from KHIC technical assistance, the financing was also critically important to their success. Several entrepreneurs received equity investments from Kentucky Highlands, capital that was not available from any other sources in the region. Other entrepreneurs indicated that they were unable to get debt financing from local banks until Kentucky Highlands became involved in the deal. In addition to the first round of financing, several entrepreneurs pointed to the importance of the follow-on capital that Kentucky Highlands was able to provide as their businesses grew or struggled and needed additional financing. Another common theme among the entrepreneurs interviewed focused on Kentucky Highlands' "staying power" in a deal, i.e., KHIC's flexibility and willingness to stick with an entrepreneur as the business experienced difficult times. This "staying power" included providing management or technical assistance as well as stepping in with an additional infusion of capital to get the business through a rough period. In one case, Kentucky Highlands was working with an entrepreneur going through bankruptcy proceedings while at the same time discussing how KHIC might be involved in his next business opportunity. In another case, KHIC served on the board of a company as the board encouraged the company to change directions and pursue a new market. Kentucky Highlands stood by the company and showed confidence in the management and the future direction. A final theme that emerged from the entrepreneur interviews was that Kentucky Highlands was the principal, and often the only, entrepreneurial support organization used by the emerging business. A number of entrepreneurs indicated that they would not have started their businesses without the involvement of KHIC. While many of these entrepreneurs eventually acquired bank financing and a few took advantage of state tax credit programs, very few of them sought assistance from other economic development organizations in the region. In most cases, the engagement of other financial or assistance providers was the result of Kentucky Highlands' efforts to bring additional partners or pools of capital to the table. These experiences confirm the role of KHIC as a lead entrepreneurial support organization in the region".*

Markley & Barkley, March 2003, page 12.

It is also clear that KHIC's efforts in obtaining and managing the Federal Empowerment Zone program for the three selected counties of southern Kentucky have had an amazing effect on rural economic revitalization and development. After the ten years of operation of this KHEZ program the following achievements were realized:

- The three-county area experienced population growth for the first time in 50 years. From 1994 to 2004 the population of the KHEZ grew by 7.9% compared to just 3.2% for the state as a whole.
- From 1994 to 2004 unemployment rates in the KHEZ zone dropped by 32.8% compared to a decrease of 5.4% for the state and a 1.9% national increase.
- There was a 29.5% increase in people who have at least a high school diploma or GED, compared to a 21.2% increase in Kentucky and a U.S. increase of 6.9%.
- From 1990 to 2000, the poverty rate decreased by 31.1%, compared to a drop of 16.8% in Kentucky and a 5.3% decline nationally.
- The average wage per job increased 38.3% and gross income rose 35.1% – both are higher than state and national average increases.
- The average number of aid to needy family cases dropped by 69.4%, and payment amounts decreased by 71%.
- Over the 10 years, the KHEZ Development Venture Fund approved 74 loans and 45 equity investments totalling more than \$33.7M including \$12.8M in repaid loan funds. This investment leveraged an additional \$122M in private investment.
- The \$6M in EZ program funding that was targeted for infrastructure leveraged an additional \$50M in infrastructure funding from other sources.
- 3,658 new jobs were created through EZ funding; 6,153 new jobs in total during the 10 year period.

## SUMMARY

Certainly the success of the Kentucky Highlands Investment Corporation over the past forty years demonstrates that with strategic action rural economic revitalization can occur, even in very poor rural regions facing very significant economic challenges.

The experience of the Kentucky Highlands Investment Corporation would indicate several important conclusions:

1. Low levels of economic activity and business development in chronically poor and economically underperforming areas are not necessarily due to a lack of economic or business opportunities per se in these regions – but rather a lack of entrepreneurs, business development support and business financing that allow economic opportunities to be identified and acted upon.
2. Economically depressed rural areas are not well served by traditional forms of business development support and traditional sources of private sector business financing. To economically improve these regions some form of non-profit or government funding assistance is initially required to fund entrepreneurial and business development.
3. If done appropriately, initial non-profit and/or public funding for business and economic development in economically depressed areas can attract and leverage very significant levels of private sector investment.
4. Given the economic and business development challenges of operating in economically challenged rural areas, an integrated approach that includes entrepreneurial development, technical business development, professional business management mentoring and the provision of higher-risk business financing will improve the likelihood of business success and ultimately economic revitalization of a region.
5. As demonstrated by the Kentucky Highlands Empowerment Zone program, amazing economic and community revitalization results can be achieved in the most challenging rural areas if a large scale, long-term, strategic and holistic rural economic development approach is implemented. The KHEZ program clearly demonstrates that when done effectively, government supported rural economic revitalization initiatives cannot only revive a rural economy but ultimately can actually “save” governments significant levels of funding that would otherwise need to be spent on social support and community mitigation expenditures.



## Further Information is available at:

- KHIC Website: [www.khic.org](http://www.khic.org)
- KHIC Annual Newsletters: [www.khic.org/annual\\_newsletters.html](http://www.khic.org/annual_newsletters.html)
- Kentucky Highlands Empowerment Zone 10 Year Report: [www.khic.org/library/cms/Image/KHIC%2010%20Year%20Report.pdf](http://www.khic.org/library/cms/Image/KHIC%2010%20Year%20Report.pdf)
- D. Markley & D. Barkley "Development of an Entrepreneurial Support Organization: The Case of the Kentucky Highlands Investment Corporation." Center for Rural Entrepreneurship, March 2003. [www.energizingentrepreneurs.org/content/chapter\\_5/stories/1\\_000088.pdf](http://www.energizingentrepreneurs.org/content/chapter_5/stories/1_000088.pdf)

## APPENDIX 1

Excerpts from the KHIC case study "Development of an Entrepreneurial Support Organization: The Case of the Kentucky Highlands Investment Corporation" by Deborah Markley and David Barkley, Center for Rural Entrepreneurship; March 2003.

### Lessons Learned

Kentucky Highlands provides a useful model for identifying lessons learned because of its long operating history and the evolution of its program portfolio over time. There are, however, important caveats to this experience that must be acknowledged. First, KHIC received substantial public (federal) investment at its inception, funding that is unlikely to be available to programs created today. The capitalization of an entrepreneurial support organization is a significant challenge that must be considered. Organizers of an ESO will need to devote resources during the start-up phase to raising capital from a variety of sources including public, private, and non-profit. Second, KHIC provides assistance to entrepreneurs who the staff identifies as being viable candidates for investment. KHIC may work with an entrepreneur to develop a business idea to the point of being investment ready; however, the organization does not attempt to identify potential entrepreneurs who articulate an interest in starting their own business but who present no concrete business idea. There continues to be a gap in the region in providing this deal flow development activity. While this development is occurring in specific parts of the region, such as in the Jackson County Entrepreneurship Center, it is not widespread throughout Appalachian Kentucky. The following lessons learned are offered as input to other organizations serving rural regions that are interested in developing effective ways to support entrepreneurs and encourage economic development. The uniqueness of rural regions suggests that no single model will be applicable in all places. As a result, the shared learning from Kentucky Highlands can be applied to other

models of entrepreneurial development and should be viewed as guiding principles for other organizations to use as they create their own unique strategies.

### Lesson One: Focus on Entrepreneurs and their Enterprises

The focus of Kentucky Highlands' activities is on the entrepreneur and his or her enterprise, not the capital used to support the entrepreneurs. KHIC works with individual entrepreneurs to put together a package of assistance that will increase the probability of the new business' success. This assistance includes recognizing the weaknesses in an entrepreneur's set of management skills and plugging the gaps in the management team, even with KHIC staff. Staff members are committed to making the entrepreneurs and businesses in which they invest successful, and the KHIC staff invests in businesses that they can run if necessary. The willingness to step into a management position and work side-by-side with entrepreneurs to turn a business around differentiates the Kentucky Highlands model from the typical venture capital or business investment model. As an example, KHIC Vice President for Investments, Elmer Parlier, assumed the duties of president in one of KHIC's portfolio companies, working along with the company's president. Through his efforts, the company instituted changes that put the business on the road to profitability. Control of the company then reverted back to the president. This ability to fill a gap in an entrepreneur's management team, even as high as the president, is particularly important in a rural region like southeastern Kentucky where the pool of potential management talent is limited. This hands-on technical assistance also helps to build the skill set of the entrepreneur and the ability to manage a successful company in the future.

### Lesson Two: Committed and Skilled Staff

The quality of support provided to entrepreneurs is a function of the quality of staff assembled in the Kentucky Highlands organization. Individual staff members demonstrate a strong commitment to both the southeastern Appalachian Kentucky region and the organization itself. Many of the senior management staff have been with the organization for more than 10 years and have been in the region even longer. The current staff averages 9.5 years of service. This longevity helped KHIC maintain a strong focus on and commitment to the organization's mission. The Kentucky Highlands staff brings a set of diverse skills to the mission of assisting entrepreneurs. Staff members who work directly with entrepreneurs have technical skills, such as accounting, along with experience managing business enterprises. This business experience is essential to KHIC's mission since staff can assume management of a portfolio company as needed in order to turn a company around. This blend of deal making and business management skills is important for working with the more inexperienced entrepreneurs that seek assistance from KHIC. A primary



concern for many ESOs is management succession. Most ESOs are created by individuals who are dedicated to serving entrepreneurs in a particular distressed region. For example, there is a missionary zeal evident among KHIC's long time staff. Maintaining staff quality and commitment over the long term, however, is a potential problem for entrepreneurial support organizations. KHIC addresses this issue in two ways, by developing local talent and by compensating staff adequately. KHIC recruits interns from local colleges to work in the organization and then actively encourages those with talent and commitment to return after college. This cultivation process has provided them with additional staff people as needs developed. Currently, at least three of the eleven business development and office staff came to KHIC through internship opportunities. In terms of compensation, KHIC staff has an opportunity for some profit sharing as well as salary packages that compare favorably with other economic development organizations. However, Kentucky Highlands is not in a position to offer compensation packages in line with more traditional venture capital funds, limiting their ability to attract staff from these institutions.

### **Lesson Three: Focus on Grantsmanship**

Grantsmanship is a key function within the KHIC organization. KHIC has been successful in tapping a number of federal programs (as described above) that provide greater flexibility in responding to an entrepreneur's needs. The success in raising grant money is a function, to some extent, of the specialization of senior management. The CEO of the organization has an explicit focus on grantsmanship while the COO and Vice President focus on deal making, deal development, and entrepreneurial assistance. While this specialization evolved over time as new leadership was brought into KHIC, it can serve as a model for other organizations. However, grantsmanship does require a commitment of organizational resources. Both time and talent are required to identify potential sources of grant/program dollars and complete the applications required. For example, the EZ program application process took ten weeks to complete, requiring almost complete focus on the part of several staff. Jerry Rickett, CEO, devotes most of his time to grantsmanship so that Kentucky Highlands has one FTE devoted to this function. While KHIC has been successful in expanding the resources and tools available to help the region's entrepreneurs, it is important to recognize the significant commitment of resources required. In addition, Ray Moncrief noted that public funds to capitalize an organization similar to Kentucky Highlands are more limited today. Other resources, such as private and philanthropic dollars will have to be targeted as well.

### **Lesson Four: Active and Supportive Board**

The KHIC Board of Directors played and continues to play an active role in supporting the organization's mission. As with the staff, the continuity and longevity of the Board has helped KHIC maintain

its focus on helping entrepreneurs within the region. The current Board averages 17.3 years of service per director. Wayne Stewart, the past president of the Board, served for more than 25 years. The Board challenged KHIC to be innovative and try new approaches to encouraging economic development in the region through support of entrepreneurs. According to Jerry Rickett, the Board encouraged KHIC staff to take risks and have an impact on the region. Rickett was asked each year what new thing the organization was going to try and what its two biggest failures had been. If there were no failures, Stewart felt that KHIC was not achieving its mission of taking risks to create sustainable businesses in the region. The organization of the KHIC Board changed over time in an effort to provide ongoing and politically neutral support of the organization's mission. Initially, Board members were elected by the six community action agencies that founded KHIC, in keeping with the original funding – the Office for Economic Opportunity - agent's requirement that the poor have an opportunity to participate in the governance of the organization. However, as Kentucky Highlands' focus shifted over time from community development to a capital-led economic development strategy, it became more important for the Board to have greater control over its membership. The Board needed members with a deep understanding of the organization's mission and a commitment to KHIC's investment strategy. As a result, the Board became self-perpetuating in 1981, and the remaining members of the Board select replacements for open seats. This new structure provides insulation for the Board from the political process since Board members are not appointed by county-level organizations. The level of Board commitment to KHIC is high. Bill Singleton, current chairman of the Board, indicated that Board members have been focused generally on Kentucky Highlands' mission and not very much on self-interest. The Board members are very dedicated and have established strict participation requirements in order to retain a Board seat. Singleton also indicated that Board members generally feel that serving on the Board is a meaningful experience and that they are giving something back to the region. This level of commitment has been critical to the success of KHIC.

### **Lesson Five: Partnering to Create an Entrepreneurial Region**

The organization's success over time encouraged the formation of other local development organizations and helped to create a more entrepreneurial region. Kentucky Highlands was influential in the creation of a number of development organizations within the region, including MACED and the Appalachian Development Alliance. At the same time, partnerships are a key to KHIC's success, allowing the organization to share risk, extend its geographic reach, and increase the talent pool available to help entrepreneurs. Partnerships also permit market segmentation so that KHIC can focus on the larger deals and existing entrepreneurs while other organizations target smaller deals and potential entrepreneurs. In addition to partnering with regional organizations, Kentucky Highlands has developed a significant network of national partners. KHIC works closely with the Rural Local Initiative Support Corporation, the

National Congress for Community Economic Development, the Community Development Venture Capital Alliance, the National Community Capital Association, the National Cooperative Bank and others. These partnerships help strengthen Kentucky Highlands and bring additional resources into the southeastern Kentucky region. While initially KHIC may have been viewed as the “big brother” among regional development organizations, the capacity within the region has improved over time. Other regional organizations have expanded in size and experience. These organizations have had time to build relationships so that individual organizations are thinking about partnering as opposed to going it alone. As a result, the partnerships among these different organizations create an entrepreneurial support infrastructure that no single organization could provide.

## **Conclusions**

Kentucky Highlands has a long history of supporting entrepreneurs and providing capital to create new business enterprises in the southeastern Kentucky region of Appalachia. The organization has evolved a set of programs over time that provides a range of capital products and technical services to area entrepreneurs. Kentucky Highlands uses the developmental venture capital model to promote economic development in its service region. If the organization’s success is measured against the standards of venture capital funds, in terms of rate of return achieved, Kentucky Highlands’ returns are not in line with those of more traditional funds. However, as a self-sustaining economic development organization, supporting entrepreneurs and their businesses and creating jobs and wealth in the region, Kentucky Highlands has been highly effective. According to former president Miller, Kentucky Highlands has been entrepreneurial itself – finding creative, innovative solutions to the challenges the organization has faced as it pursued its mission. While the organization’s orientation and programs have changed over its history, the focus on creating jobs and locally controlled wealth by investing in entrepreneurs and their business enterprises has not changed. Kentucky Highlands’ success is a product of a committed and skilled staff, a dedicated and active board, an explicit focus on grantsmanship, and a willingness to partner with or encourage the creation of other regional development organizations focused on building the entrepreneurial capacity in the region. KHIC’s capital-led strategy is just one means of encouraging entrepreneurial development; however, the lessons learned from Kentucky Highlands experience apply to other economic development organizations that are committed to becoming effective entrepreneurial support organizations in their rural regions.