

2. Why Business Incubation?

Understanding the role that SME's play in the national economy and providing them with adequate office space doesn't explain the value proposition of this initiative, or what makes it so unique. Young companies are particularly vulnerable in their early/start-up years, and particularly in Africa where there is a higher percentage of inexperienced workers starting businesses. A lack of exposure to the formal sector's mature corporate governance (due to a widespread lack of employment opportunities) means that there are a significantly higher percentage of students or inexperienced entrepreneurs trying their luck at starting companies. ICT start-ups tend to attract technology professionals with little business experience. Further, the start-up environment can be significantly more hostile in a developing economy, where services remain inadequate, inaccessible or expensive. In a report quoted by the US Small Business Administration, the data shows that, across sectors, 66 percent of new establishments in the US were still in existence 2 years after their birth, and 44 percent were still in existence 4 years after¹. Other analysts claim failure rates as high as 60 percent in the first five years and some anecdotal evidence in South Africa would even suggest it may reach up to 80%.

Although these rates remain controversial, it's broadly accepted that incubation programmes can increase survival rates dramatically when programmes are well-run and start-ups pay for services: "Our experience has shown a success rate of 75-81 percent for companies participating in our incubation programmes" says Jill Sawyers, of The Innovation Hub in South Africa. Similar results are found at the Bandwidth Barn in Cape Town (started in 2000) with a tenant success rate of 65%: "In the past five years, of the 142 businesses that have passed through our doors, 111 of them are still in operation. This overall success rate is astonishing considering that most companies come to the Barn with little more than a laptop and a dream," (Odette Potter, general manager of the UUNET Bandwidth Barn). In addition to the provision of physical space, clearly there are critical interventions that can be made by incubator programs that significantly help these individuals, such as management coaching, mentors, help in preparing effective business plans, administrative services, technical support, business networking, advice on intellectual property, and help in finding sources of financing.

It is clear that the critical success factors for these incubators include:

- **volume** of companies co-located is important as it leads to natural clustering & collaboration
- entrepreneurs will **learn more from each other**, and other businesses, than 'consultants'
- **combining start-ups with mature companies** in same building encourages collaboration
- **diversified** models (incubation + office rentals) keep programs sustainable and independent
- not being 100% publicly funded keeps incubator **focused** on tenants and services provided
- strict **entry criteria** (focused on innovation & implementation) can ensure high success rates

¹ Survival & Longevity in the Business Employment Dynamics Database" Amy E. Knaup, Monthly Labor Review, (May05)

- investors/entrepreneurs seeking to make new equity investments can be **leveraged as mentors**
- businesses seeking future clients can provide **discounted** professional services
- a **strong manager** who monitors both mentors and companies is key
- use managers who have **entrepreneurial experience** and can ‘relate’
- incubation programs can remain lean and **cost effective** with few employees (2)
- ensuring tenants **pay for services** screens out those that are not somewhat commercialized
- incubators create a **climate of collaboration** & networking from the start

3. What Challenges do SMEs face?

Small and Medium sized businesses across Africa face many and varied challenges to their growth and operations. Incubation projects are designed to address the following challenges, which are particularly acute for ICT enterprises:

- Appropriate office space
- Appropriate support services
- Professional networking

Appropriate office space

Poor electrical & water: SMEs need first and foremost an appropriate infrastructure in a building. This consists of dependable and redundant power supply, appropriate electrical installation, power conditioning for sensitive equipment, and water. This is rarely available in the cheaper office rentals that most start-ups and small enterprises can afford.

Expensive Internet: ICT SMEs need good and low cost connectivity to the internet backbone; preferably a fibre optic connection that has less interference or latency than a wireless/satellite link. Most SMEs need to arrange their own wireless or DSL data links which prove to be less reliable and more expensive than if they could pool resources and demand and push for wholesale pricing on bulk connectivity options.

Inflexible lease terms: leases can often be paid as much as three years in advance and do not provide flexibility in terms of changing the terms of the lease, or expanding or contracting into additional space as the company grows or contracts.

Individual Resources: companies generally have to provide their own resources, like generators, receptionists, security, kitchens, water tanks, internet connections as they cannot rely on other building tenants for maintaining shared resources. An ICT SME is going to be much more vulnerable to downtime than other SMEs – it’s like a factory, no power, no income. ICT service industries supporting global customers need a 99% uptime. Building your own infrastructure and environment in an older building is expensive to setup, and expensive to maintain.

Unattractive locations: SMEs will often locate in the cheapest real estate available and this can project a negative image to potential customers – often taking a garage or floor of a house, or locating in a crowded market area. Image is important for an aspiring SME trying