

Small Enterprise Development International, London

CROSS FIRE: Incubators: timely assistance or a waste of funds?

First salvo, February 2001

Dear Rustam,

Greetings and best wishes to you. We haven't met, but I feel like I know you, since several places where I've worked around the world, I've had to spend time explaining to people why incubators you've been promoting are not the wisest use of their scarce resources. Here's why.

I've spent most of the past 25 years trying to understand opportunities and needs of micro and small enterprises. In thousands of conversations and survey responses, entrepreneurs tell me their needs are three: 1) markets: information about products people want to buy, and who is buying; 2) improved capacity to supply those markets; and 3) finance, for capacity building and working capital to supply those identified markets. The order is crucial; good interventions start from market opportunities and work back from them.

Incubators generally leapfrog that approach, supplying one particular type of help, infrastructure and work space -- which entrepreneurs almost never identify as their most pressing need -- often at very high cost per beneficiary. I'm sure there are places where they are just what the doctor ordered; but in the many places I've worked, I haven't found any yet.

I have several other problems with incubators, but I suppose I'll have a chance to tell about those after you've explained why they are the best thing since sliced bread!

Sincerely,
Don

Dear Don,

Let me start with one point on which we agree: The proper identification of the market for an enterprise is the first essential step. But the majority of businesses skip this, with unfortunate consequences. This is also true of many incubators and other business development services .

Now to our differences: all small business services put together serve only a miniscule proportion of the total small enterprises in a country. Depending on entrepreneurial needs, local conditions and culture, there are indeed situations where a well-designed and well-managed incubator can provide the counseling, training, networking, and work space required, with sustainable results.

You refer to 'micro and small enterprises'. But in the developing and restructuring countries where I work, most of the incubators serve technology-related, early-stage businesses, selected for their growth-potential and innovation.

Finally, you say that in the many places you have worked you have not found any where incubators are useful. Perhaps you have not looked in the right places, or your yardsticks for assessing performance compare apples to pineapples (or sliced bread to tortillas!)

Sincerely,
Rustam

Second salvo March 1, 2001

Dear Rustam,

Great! Now we're getting to the interesting part! You say, there are situations where a well-designed and well-managed incubator can provide sustainable results. In doing so, you suggest it will generally serve technology-related, early-stage businesses, selected for growth potential, providing counseling, training, networking, and work space. All this must come *after* a proper identification of a market, 'the essential first step'. No wonder I haven't seen incubators that meet all those conditions!

This list leads directly to issues of costs. Providing counseling and training for early-stage businesses (that may need a lot of each) in high-tech areas (where skills are specialized, counselors/trainers have good options) can make such facilities expensive. Will trainers continue to stay on the frontiers, crucial in high-tech markets? How many enterprises will actually benefit?

One wonders why such capacity-building services need to be provided in concentrated locations (i.e. in incubators). How much, and over what time period, do all these need to be subsidized, when each is often already available in the market? How can they be provided in ways that strengthen rather than undermine existing markets for such services?

I look forward to your thoughts!

Cordially,
Don

Don,

Let me respond to the points raised in your latest salvo.

First, you are concerned with the high costs of providing counseling and other services. Compared to what? And with what commensurate benefits? A good incubator provides basic support from its in-house team but accesses specialized services from external networks, from *pro bono* sources including mentors on its board and private business, from faculty and facilities at universities to which many are affiliated.

Then, you wonder why such services need to be concentrated under one roof?. Because there is synergy in sharing experiences and bartering/buying between clients. Because the convergence of services can be more effective than buying each item, *a la carte*. Because start-up entrepreneurs have scarce personal or family resources for renting smart space and office equipment/facilities, which the incubator offers.

Finally, you ask how can the services be provided in ways that strengthen rather than undermine existing markets?. Well, in many developing countries the private service providers are now emerging, and a local incubator can better manage to meet the demand than a publicly-funded small business center. Besides, as noted above, incubators complement the market, not compete.

Don, innovators do have crazy ideas but they are not stupid. Nor are the governments and donors that help subsidize initial incubator costs, in rich countries and poor. A quarter million businesses have gone through the incubation process to date at some 3,000 incubators world-wide, mainly because incubators fill a niche, enhance the chances of new venture survival and success, return to the exchequer many times the net subsidy in taxes, and provide a variety of other benefits.

Sincerely,
Rustam

Third salvo, March 2001

Dear Rustam,

The intuitively appealing argument about the synergistic advantages of concentration leads to two questions. First on the nature of the concentration, most of the advantages you mention can be achieved without the enterprises operating under one roof. Lots of concentration happens all by itself, as similar businesses group together in one part of a city. Many types of high-tech businesses interact well via modem. How much does a common roof add to that? Second, while I have often heard the argument made about the benefits of such groupings, all the many attempts I have seen to measure those benefits have come up empty. So far, I think, the reasoning rests on anecdotes and a priori assertions.

My other set of puzzles concern the circumstances under which incubators might be most likely to make a contribution. I have read about incubators started in the newly independent states of Eastern Europe and in Latin America. Since I have never worked in either area, I have no way of judging their effectiveness there. If incubators meet a real need in such places, are they different in some important respects from the cities and towns of Africa and the Middle East where I have done most of my work and where, as far as I can tell, they have never been an effective development mechanism?

So much more to say, so little space! In the end, I finish where I started. Based on what I have seen and read, I find that incubators are high-cost interventions that do not meet the most urgent needs of most small enterprises. Yet people whom I respect, including some such as yourself who have spent years designing and supervising their operations, argue that, *in certain circumstances*, incubators constitute an effective – and even cost-effective – means of helping *certain types of small enterprises* perform effectively. I can only ask on behalf of those of us who remain skeptical that you help focus the debate by specifying the types of enterprises and the types of locations where incubators are most likely to make a contribution; and provide quantitative studies that demonstrate the effectiveness of the best existing projects. While I am ready to be convinced, I am afraid that, so far, the evidence is all on the other side.

Rustam, any thinking person knows that my task in this exchange has been much easier than yours. It's much easier to ask difficult questions than to try to defend a controversial approach! I take my hat off to you for your valiant job. I have enjoyed the exchange.

Cordially,
Don

Dear Don,

You agree that the clustering of business firms can be helpful and then argue that this is happening anyway, even without incubators. Yes, in some respects, but not in many others as we discussed earlier.

You ask about the special circumstances for the success of incubators as you have not encountered effective ones in towns of Africa and the Middle East where you worked. The conditions for good location and pre-requisites for success include a place with the supportive state policies and business infrastructure for venture creation, patient stakeholders with consensus on objectives and expectations, preferably a vacant work space for no-frills renovation, a knowledge base of innovation and entrepreneurship development, a strong services-focused management team, and at the outset a feasibility process which will prepare for (not guarantee) success.

You ask again for quantitative studies and hard evidence. I am reminded of a movie I saw many years ago. It was about the miracles at Lourdes and started with the statement:

"For those who believe no explanation is necessary.

For those who do not, no explanation is possible".

I do not suggest that incubators can perform miracles, and I do agree that evidence is essential on the additionality provided and the outcomes of **all** business support services; hence the serious search for better ways to measure, appraise, benchmark and evaluate performance. Till the evaluators come up with objective assessments, we are entitled to some skepticism.

Don, I have valued your comments. We have, I think, expressed our views with candor and professionalism, based on our experiences as development practitioners, not crusaders. We have, I hope, a better understanding of the problems and potentials. I do.

Cordially,
Rustam