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Incubator Sustainability

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What's the rationale for incubation?

- Arguably, the primary rationale for incubation is to **correct market imperfections**
 - High costs and risks of serving SMEs relative to larger firms leads to lack of access to resources by SMEs
 - Incubation, like education and public health, creates external economies, the economic value of which are not reflected in the returns to a private business
 - Market imperfections are especially common in developing and transitional countries
 - Incubators are growing most rapidly in these countries
- Because incubators step in where markets fail, it makes sense to run them as non-profit entities

There may be a trade-off between sustainability and impact

- Put in other words, we should evaluate the performance of incubators first on the basis of their contribution to the development of small businesses ("impact"), and only afterwards on their financial self-sustainability
- Microeconomic efficiency (return on private investment) must be weighed against macroeconomic impact (return on public investment)
 - The appropriate balance between microeconomic efficiency and macroeconomic impact should be decided on a case-by-case basis

Many ways of looking at “sustainability”

- Some alternative definitions
 - Incubator depends only on assured subsidies to cover operating expenses
 - Incubator requires no subsidy to cover operating expenses
 - Incubator requires no subsidy to cover operating expenses and build up contingency fund
 - Incubator requires no subsidy to cover both operating expenses and startup capital costs
- Only the last definition makes economic sense
 - Clearly, sustainability will depend on the size of the income stream created by the initial investment
- But as the previous slides argued, sustainability is not the primary objective of business incubation

But there may also be independent arguments for sustainability

- Setting an example for client entrepreneurs
 - Incubators cannot help client businesses to act entrepreneurially if they do not themselves act entrepreneurially
- Reducing incubator vulnerability and maximizing impact of scarce public resources
 - Incubators that are not sustainable risk failure if sources of subsidy disappear
 - Like its clients, the incubator should be “incubated” for 3-5 years and then become self-supporting

Some Practical Considerations

- Everyone understands the principle of paying for tangibles, like rent for workspace
 - Providing attractive and marketable workspace and physical facilities is often critical to incubator sustainability
 - Rental income should provide a surplus to the incubator in order to subsidize other operations
- Small businesses worldwide are unwilling to pay market prices for intangibles like business advisory services
 - Some services like accounting, legal, website development, etc, are more tangible and easier to charge fees for
 - Strategic services like business plan development are often best bundled with rent



Thanks!

Questions? Comments?

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