



Incubators as a Potential Local Economic Development Tool

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Incubator Development

Over the past twenty years, there have been many changes in our national economy. Employment growth has shifted from manufacturing to services and from larger firms to small businesses. Also small businesses have become the center of innovation. Small businesses account for approximately 75 percent of the net new jobs in the U.S. economy and produce 13 to 14 times more patents per employee than larger firms (Leebaert, 2006). With increased importance placed upon small business as a vehicle for economic development and innovation, business incubators have been created to assist in the development and maturation of small business.

The National Business Incubator Association (NBIA, 2005) estimates that in excess of 900 business incubators are currently open in North America with 3,500 operating worldwide. Over 13,000 clients, affiliates, and graduates have been served by these incubator programs and over 85% of businesses that had started through an incubator are still in operation (NBIA, 2005). Overall for small businesses, the failure rate is 80% during their first four years of operation (Weinberg, 1987). Given the high success rate of incubated small businesses, it is evident why small business incubators have become so popular as an economic development tool.

A small business incubator is a facility that offers adaptable space and support services at a discounted rate. Incubator support services include office space, financial assistance, and management training. Most incubators are designed to house multiple tenants, thereby reducing the individual cost to tenants of acquiring support services. Incubators are designed for flexibility and supply space, which can easily be adapted to meet the needs of many types of operations. This permits the tenant firm to allocate resources and time to the development of a product and become established in the market.

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Office support provides incubator tenants access to office equipment and services they could not afford otherwise. The multi-tenant facet of the incubator allows the cost of the equipment to be spread across several tenants, thus reducing the cost to each tenant. Tenants usually pay as they go when using the equipment. Access to a copying machine, fax machine, secretarial support, or a computer can greatly aid a small firm in the management of their office.

Financial support provides tenants with access to much needed capital to improve their firm. Financial support can range from venture capital and micro-loans to assistance with securing commercial loans with an existing bank or other financial institution. This assistance is important to high technology operations that are usually very expensive to start and operate.



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The NBIA study (2005) indicates that successful incubator programs provide resources beyond a reception service and copy machine. A successful incubator must have on-site staff to coordinate and deliver business assistance to client businesses. The assistance also needs to be sophisticated enough to mentor client businesses to self-sufficiency within a set period of time.

Incubators also provide an environmental benefit. By housing many entrepreneurs in close proximity, tenants can assist each other with problems. This "support" group improves the firm's chances for survival.

Nevada Incubators

Nevada's history with incubators is somewhat limited with only one currently operating in the community of Henderson, Nevada. The Henderson Business Resource Center provides business development expertise to new and growing businesses in southern Nevada. With the rapid population and business growth in the state of Nevada, many economic development practitioners have enquired as to the use of business incubators to encourage small business growth in Nevada. Also, the U.S. Forest Service has been interested in incubators for development of a small diameter wood industry in rural Nevada.

Incubator Consideration: Four Key Questions

When considering business incubators several key questions should be considered by local economic development practitioners. This fact sheet is designed to assist communities that are considering incubators for local economic or product development. Key questions related to the demand, management, and community support are discussed. Steps in incubator start-up are discussed, followed by incubator marketing strategies.

- **Is there sufficient demand for an incubator and/or the services which an incubator provides?**

Does the demand exist for the services that an incubator provides? This information can be acquired by surveying the people and agencies that deal with small business owners and people who are potential entrepreneurs. This includes agencies such as banks, chambers of commerce, county extension offices, realtors, and others who are often approached by people needing information about starting a business. After it has been determined that there is sufficient demand for the construction and continued operation of an incubator, then the next question should be answered.

- **Is the managing agency committed to the success of the incubator?**

The incubator houses firms which require a high level of management assistance. The managing agency will be required to meet the needs of these firms and to utilize available resources to keep the incubator in operation. For the incubator to be successful, appropriate resources, efforts, and assistance will have to be offered. If the incubator management entity decides to go forward with incubator development, the next question is important.

- **Is there a suitable site where an incubator can be built or renovated that is convenient to potential tenants and existing businesses/markets?**

The incubator site is a highly crucial factor in the success of an incubator. A site should be easily accessible to potential tenants as well as potential customers. An accessible site lends itself to success. Tenants need to feel at ease with the facility and not have to worry about their customers finding their business. Customers prefer a business place that is easy to locate. Site selection can also impact the cost of the incubator program. For example, will an existing facility be renovated or will a completely new building be built? Once the site and facility type are selected, there remains one more key ingredient for incubator success.



- **Is there community support for the incubator idea?**

Incubators are designed to foster new and viable small firms by reducing their costs and providing them with management assistance. This is good for the tenant firm; however, existing firms may feel threatened by the incubator. The existing firm may feel that the incubator is providing an unfair advantage to its competition. After all, firms that are launched from an incubator receive aid that will help them survive and compete in the market. Community involvement is essential in the smooth operation of an incubator. The community should be informed about the incubator and play some roll in its development and operation. It is important to match the needs of the community with the goals and objectives of the incubator. This matching is best accomplished by creating an incubator advisory committee made up of local officials and business persons. The purpose of the advisory committee is to review incubator practices such as tenant selection. Judicious tenant selection can help prevent undue competition and too much of a particular business product or service.

Incubator Start-Up

Once the decision to develop an incubator is reached, there are six basic steps in developing an incubator. The essence of these steps is summarized from a publication by Peter Bearse (1993).

1. Conduct a market analysis.

An accurate market analysis is the keystone to the development of the incubator. The market analysis identifies potential tenants and the demand for an incubator and the services which it provides. If it is done accurately the analysis will help to define the needed incubator facility and its services. This is done by measuring the size and needs of the market. Size of the market will determine if there is sufficient demand for the construction and ongoing operation of the incubator. Needs of the market can mold the services and programs of the incubator.

2. Select an incubator site.

The incubator site plays an important role in the success of an incubator. Depending on the decision to renovate an existing facility or to build a new one, the site selection process should occur based on the convenience to potential tenants and their customers. An incubator site should be attractive and project an image of success. The decision to renovate or build a new facility should match the incubator's goals as well as the needs of the market and community. Renovated facilities are typically cheaper per square foot than new facilities. Typically, renovated facilities are aimed at providing affordable space. New facilities are designed to focus on the provision of support services. If a community has a large potential clientele and thus, a large demand for inexpensive space, a renovated facility will best serve this need. On the other hand, if a community does not have an obvious client pool, thus less of a demand for space, a new facility might be more suitable. In a study of Oklahoma incubators, Rushing and Woods (1995) found that the location of a majority of incubator sites in Oklahoma was due to the proximity of a vocational-technical school.

3. Facility design.

Once a facility site and building are selected, it is important to review the design of the facility for convenience factors. Convenience factors are arrangements in the building itself. Important factors include the location of corridors and loading docks. Tenants should have easy access to loading facilities. Location of office services, incubator personnel, and other services are also important to operation by the tenant. Facilities should be designed for easy occupation by a variety of tenants. Ease of adaptability of tenant space is important to reduce the downtime facing a tenant who is moving into the incubator. All of the factors dealing with the move into and operation of the business within the incubator should be reviewed prior to construction or renovation. Nationally, the majority of incubators were built specifically for use as an incubator (Allen and Daugherty, 1987). Successful incubators are well designed to expand the tenant's access to their customers.

4. Selection of support services offered by the incubator.

What will the incubator offer to potential clients other than inexpensive space? Determination of the type and range of services is important. Incubators must be prepared to cater to the needs of several types of potential clients. Also, incubators should consider how these services are to be financed. Will tenants pay for these services or will the incubator sponsor pay the provisions? Part of the financial planning for services needs to include the possible subsidizing of these services. Some incubators subsidize their services to further relieve the financial burden placed on their tenants. The funding source for this subsidy should be incorporated into the service plan.

The types of services desired by potential clients are an important part of the market analysis. Rushing and Woods (1995) asked Oklahoma incubator managers, tenants, and graduates to rank the most important business incubator service offered. The three most important services from each group are as follows:

Managers

1. Management assistance
2. Duplicating
3. Machinery and equipment

Tenants

1. Management assistance
2. Machinery and equipment
3. Duplicating

Graduates

1. Management assistance
2. Duplicating
3. fax

Rushing and Woods (1995) also found that business incubator services were limited by available funds. Therefore, when establishing a business incubator, developers must plan for the funding of necessary business services so that the incubator can efficiently service its tenants.

5. Prepare an incubator financing plan.

The financing plan will provide projections of how the incubator will operate for a five to ten year period. This plan must be created with reliable assumptions. Faulty estimates will nullify the effectiveness of the plan and



jeopardize the soundness of the incubator. A financing plan needs to address how immediate and long-term capital needs will be met. The financing plan should determine if the incubator will be self-sustaining after five years.

Incubators receive initial funding from a variety of sources. The most common are grants from various state and federal agencies. Incubators have even held a bond election, which is a good way for a community to show support for an incubator.

Many incubators generate operating capital from rent and service fees. Other funds for operation and facility improvement are provided by the incubator's sponsor.

6. Incubator organization and management.

Incubator goals and objectives should be drawn up in the organization phase. Incubator goals and objectives should be closely related to the goals of the community and their expectations of the incubator. Incubators may be profit or nonprofit organizations. Most incubators are set up as nonprofit. Management functions include the review of staff qualifications for the incubator. Incubator staff should possess knowledge of many areas to best serve the broad types of potential tenants entering the incubator.

Once all of these steps are completed, they should be compiled into an overall business plan. This plan should be flexible and updated with the changing conditions facing the incubator. One area not discussed previously that is important to the incubator in later operation is a marketing plan.

Effective Incubator Marketing

Attracting new tenants is crucial to the continued success of an incubator. This task is more difficult than might be expected. The first and most basic form of advertising for the incubator is location. A good location is important for public visibility. The facility should also be neat in appearance. As with other businesses, a poor first impression can be disastrous. A well-constructed and attractive sign displaying the name of the facility and the current tenant firms is an important first step in marketing. These efforts cater to the local business traffic. Other methods must be incorporated in order to attract a broader field of tenants.

A study by David Allen (1987), a professor at Pennsylvania State University, surveyed incubator contacts with respect to nine marketing tools to determine which of these was the most effective at promoting the incubator. The nine areas, ranked in order of importance, are

- Informal external network (word of mouth)
- Affiliated agency/center referral
- Current tenant referrals
- Public speaking
- Mass media
- Brochures/pamphlets

- Newspaper classified
- Radio advertising
- Television

Marketing methods that address incubator promotion to people on a one-to-one basis do the best jobs of promoting the incubator. Conventional advertising techniques fared poorly. Allen (1987) notes that the most effective marketing techniques were time intensive not cost intensive. Creating informal networks, making public presentations, and utilizing affiliated agencies takes time but is reported to be beneficial.

The best methods for marketing involve contacts and past tenants. This is difficult for new incubators that have not had time to develop such contacts. However, young incubators need to conduct operations in a manner that generates good contacts and references from their tenants. Satisfying initial tenants and making unofficial network contacts early in an incubator's life will ease the need for formal marketing in the later years of incubator operation.

For more information or help regarding small business incubators, contact the National Business Incubator Association (NBIA) and the Small Business Administration (SBA) at the following addresses:

National Business Incubator Association
One President Street
Athens, Ohio 45701
Phone (614) 593-4331

Small Business Administration
Office of Private Sector Initiatives
1441 L Street, NW (Room 317)
Washington, DC 20416

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