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Article

## The Sustainability and Challenges of Business Incubators in the Western Cape Province, South Africa

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**Abstract:** Notwithstanding the growing interest in business incubation programmes and the benefits derived from such programmes, the path is beset by numerous challenges. This paper investigates the challenges faced by business incubators (BIs) as they strive to support their clients. The study utilized a qualitative approach to collect data by way of interviews to gain in-depth knowledge and understanding of the concept and challenges of business incubators. The data were collected using structured and unstructured in-depth personal interviews, which were carried out with the respondents of business incubators in the Western Cape. The research participants for this study were limited to the business incubators on the database of a local organization that promotes small and medium enterprises (SMEs) development strategy and programmes in the Western Cape Province. All five business incubators on the database were deemed suitable for the study. The results indicated that an average of twenty-five entrepreneurs graduated from the incubation programme in the last five years. Furthermore, lack of sponsorship, production space, advanced technological facilities (prototype) and expansion to different areas were found to be among the challenges hindering incubators.

**Keywords:** business incubators; sustainability of business incubators; entrepreneurial skills; small and medium enterprises

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## 1. Introduction

Given their sheer numbers and propensity to fail, one may argue that making sure that Small and Medium size Enterprises (SMEs) are self-sustaining, would be the right step towards ensuring economic sustainability in any economy. Business incubators have been proven to provide the platform for nurturing businesses. In fact, business incubators are seen globally as an essential tool for the development of SMEs and considerable amounts of resources are invested in them today. For instance, business incubation has become a growing phenomenon in countries such as Brazil, Russia, India and South Africa according to Berge and Norman [1].

Looking back at the concept of business incubation, *Db*, *Comm* and *Acc* [2] agree that it originated in the United States of America (USA) in the 1960s as an initiative to support new SMEs in establishing and developing networks, management skills, and markets for their products and services in a creative and innovative manner. Today, a growing number of studies have established that the concept of incubation has enabled a number of developed countries to initiate business policies that support economic development and sustainable economic growth [3]. However, in developing countries, business incubators and SMEs still face a number of barriers. This is particularly true for South Africa, where business failure and high unemployment still persist.

In the second quarter of 2013, the South African unemployment rate increased to 25.6% from 25.2% in the first quarter of 2013 [4]. One may contend that venturing into business is an important step towards minimizing unemployment and, in most cases, entrepreneurs face two major obstacles to establishing start-ups: lack of experience and lack of motivation. To be successful, entrepreneurs need assistance from business incubators and other businesses within the same sector to allow for the transfer of knowledge and shared experience [5].

The study utilized qualitative methods to collect data, the researchers employed structured and unstructured in-depth interviews. The researchers made appointments with five incubation managers, and all were interviewed. It is expected that addressing the challenges faced by incubators and improving the skills of the managers of business incubators, would result in them making a significant contribution towards the client's (SMEs) development. All things being the same, this will in turn mean that these self-sustaining SMEs would be able to contribute fully towards employment and economic sustainability.

This study, therefore, aims to investigate the incubation concept and the challenges faced by business incubators in the Western Cape Province of South Africa.

## 2. Background and Problem

Although tasked with developing SMEs, business incubators often lack the necessary skills to contribute fully to the development SMEs [6]. Given that most of the management staff in business incubators may not come from an entrepreneurial background, they seldom possess the ability to meet the skills requirement of their clients [7].

Previous researchers mentioned that business incubators in developing countries face a number of challenges concerning innovation and creativity. Notable among these challenges are: lack of entrepreneurial skills, lack of venture capital, poor growth rate, productivity falling behind, aging

population, downsizing, and the lack of true entrepreneurship [8,9]. Owing to the foregoing challenges, business incubators find it difficult to uphold their mandates as development agents [1,2,10] and in, some cases, their long-term survival becomes threatened. Of course, this may negatively affect SMEs who depend on them for survival [11].

Despite the numerous resources invested in incubator programmes by government and private organizations, their impact on SMEs is not well documented, especially in the context of South Africa. Studies on incubator–incubatee challenges are quite limited. Although there has been an upsurge in the number of such studies in recent years, the discourse is still one-sided with emphasis on the needs and challenges of incubatees [12,13]. Attention is yet to be given to the challenges that business incubators face as they strive to support incubatees, even though we unconditionally expect the best results from the former. Accordingly, this study seeks to answer the following research questions:

What are the challenges faced by business incubators in the Western Cape Province, South Africa?

### 3. Literature Review

For this study, the literature was reviewed under the following headings: the origin of the incubation concept, a historical perspective of incubators and challenges faced by business incubators in South Africa.

#### 3.1. What Are Business Incubators?

Bruneel, Ratinho, Clarysse and Groen [14] note BIs as recent tools utilised to promote the creation of successful entrepreneurial companies. The concept of BIs has been in existence for and evolved over the last 50 years [15]. The first incubator was established in 1959 in Batavia, New York, in the United States, but until the 1970s, the concept was unique and the aim was to support start-up companies that needed guidance and venture capital to get their ideas off the ground [16–18]. The term incubator was derived from the basic meaning of the term *nurturing*, which is to develop, small companies in a protected environment. Moreover, incubators are managed by industry professionals, from private and public organizations, and sometimes universities also run business incubation schemes.

Adegbite [19] defined the concept of business incubation as a method of creating new small businesses by providing and nurturing SMEs in the following range of services:

- Space in fully built-up factory buildings on flexible and affordable terms.
- The provision of a comprehensive range of common services, including enterprise counselling and training, shared secretarial support, start up financing and assistance with product development and marketing.
- Strict admission and exit rules, which are designed to ensure that the incubator concentrates its efforts on helping innovative, fast-growth business start-ups that are likely to have a significant impact on the local economy. Incubation rules generally limit tenancy to a period of between three to five years, thereby ensuring a reasonable turnover of tenants.
- Hands on assistance, including Research and Development (R&D), advice and risk capital, usually through a network of external providers.

- Professional management, which involves monitoring tenant businesses closely against their business plans, and ensuring that the incubator itself operates in a business-like fashion with the prospect of becoming financially self-sufficient [15,20–23]. Therefore, the incubation concepts seek efficient and effective means to link entrepreneurial talent and to accelerate growth in a new emerging business [24].

Business incubators are mostly regarded as companies that assist the development and growth of SMEs by providing various services such as, access infrastructure, marketing, financial support and networks. While it has emerged that business incubators in developing countries face a number of challenges concerning sustainability and innovation, there is limited coverage of the challenges confronted by business incubators in South Africa.

### *3.2. Business Incubators in South Africa: A Historical Perspective*

According to Ndabeni [21], the concept of business incubation is fairly recent in developing countries and still developing in South Africa. Therefore, in the context of this research, a business incubator is described as an organization that facilitates and provides a protected environment to new, early stage and existing businesses by providing a comprehensive range of shared services and enterprise development assistance. In South Africa, business incubators are run and managed similar to developed countries like the United States of America.

Ndedi [25] mentioned that one of the elements needed for an effective and efficient contribution from institutions in the effort of dealing with the failure rate of SMEs and unemployment is the development of business incubators within universities with the objective of linking theoretical knowledge to practical experience.

Mbewana [26,27] agrees that the incubation idea in South Africa context was started in 1995 when the Small Business Development Corporation (SBDC) established similar concept, which were known as hives of industry. These hives referred to a number of workstations that were gathered together to form a cluster of workshops that were created to bridge major economic obstacles in South Africa. However, although the hives played a key role in facilitating cooperation (support-like relationship) between large and small companies, they were not known as incubators because there was no time period for a company to move out of the hive. There are a number of factors that can drive an incubator to success and sustainability in South Africa such as financial sustainability, access to SMEs (clients), access to legal support, and innovation among others [21].

### *3.3. The Challenges of Business Incubators*

The South African business landscape is characterized by two incubation drives, namely; technology centres and business incubation. Both have been established with the main purpose of stimulating economic development and sustainability, particularly in the SMEs sector [21]. Business incubators in both the developed and developing countries face a number of challenges including those to be discussed in the following sections.

### 3.3.1. Access to Entrepreneurial Management

According to Cullen *et al.* [27], selecting and attracting adequately skilled professionals to manage the business functions is a critical factor for the success of every business incubator. These researchers also pointed out that without qualified and experienced subordinates the entrepreneurial venture will encounter difficulties in being sustainable and in delivering quality services.

Nieman and Nieuwenhuizen [28] agree that one of the greatest assets of any organization is to be productive and gain continuous growth in human resources. Hence, it is very important for the incubator manager to provide creativity and innovation within the business incubation functions [22]. Thus, the provision of management direction, technical support and a consulting style to a new developing enterprise is critical to the business incubator [25]. In addition to the above discussion, one can conclude by pointing out that by investing in human capital, business incubation will be able to deliver and reach its target.

Scaramuzzi [20] suggests that for a business incubator to gain long partnership and sustainability, the incubator should consider key strategic planning components such as:

- after governance, an incubator should create a board to govern incubator activities;
- incubators should hire experienced and knowledgeable staff members;
- management team of the incubator should be made up of a director and a few permanent staff members depending on the number of incubates; and
- an incubator should attract investors and sponsor, public and private stakeholders.

### 3.3.2. Lack of Entrepreneurial Skills

There is considerable evidence that entrepreneurial ventures that lack the relevant entrepreneurial skills, technical skills, management experience, and are inflexible tend to fail [29]. Morrison *et al.*, add that a number of entrepreneurial ventures do not pay much attention to efficiency and financial education. Grimaldi and Grandi [24] point out that very often the management team within the business incubator may not have required financial and managerial skills and provide the resources to run the incubator to achieve its mission.

Lalkaka [7] argues that the inability of business incubators to deliver can be partly attributed to the fact that the managerial control does not come from an entrepreneurial background, and hence, unable to deliver the adequate support required by SMEs. Furthermore, Lalkaka mentioned that business incubators in developing countries face a number of challenges concerning innovation and creativity, which can be addressed through entrepreneurship education. Thus, Sandrock [30,31] suggested that the South African education system, including high school learners and graduates from higher learning should be taught entrepreneurial skills in order to create more employment rather than to be job seekers. Lastly, the researcher believes that with the use of entrepreneurial skills, both business incubators and incubated entrepreneurs become well-developed and sustainable.

### 3.3.3. Sustainability

The lack of growth and sustainability for business incubation is among the main challenges that could lead to a business incubator not delivering and reaching its objectives [20]. Thus, lack of growth is determined by the total annual turnover and overall number of graduates in the incubation programme. Lack of sustainability is when the incubator cannot maintain and sustain itself. This researcher adds that the ability of the business incubator manager is measured based on his or her capability to raise funds, employ qualified people and maintain the resources needed to run the incubator efficiently and effectively.

Hence, this negatively affects the primary aim of the incubator because normally, the rental and provision of space are not sufficient to cover all the cost of the business incubator [20]. Thus, for a business incubator to be economically sustainable, it is very important for the management to look for partnerships and shareholders that can provide financial support and enable the incubator to be sustainable. Hence sustainability, in this context is the capacity to achieve continuous improvement and obtaining a positive cash flow soon from partnerships and stakeholders [32].

### 3.3.4. Access to Technological Based Facilities (Prototype)

According to Caleb, Olaopa and Siyanbola [33] businesses have limited access to technology-based facilities and face difficulties in gaining access to intangible and tangible resources. Depending on the type of incubation, Ndedi [25], suggests that the aforementioned challenge is further compounded by the fact that “these incubators must also provide potential youth entrepreneurs with information on appropriate space and flexible leases existing in the market, shared basic business services and equipment, technology support services and assistance in obtaining the financing necessary for company sustainable growth”. Hence, the lack of technology-based facilities further inhibits an incubator ability to meet the needs of its clients SMEs.

### 3.3.5. Access to Funding and Sponsorship

One of the measures of good management is an incubator’s ability to attract sponsors, raise funds and mobilize resources that could be utilized to better the incubator business model in servicing incubatees [20]. This researcher concurs that in developing countries, particularly where business incubators are still evolving in obtaining the public support, and international linkage is essential during the early years of operation. International linkage in this context means partnering with other incubators and companies internationally. Grimaldi and Grandi [24] mention that public business incubators are non-profit organizations; hence they normally get incubated financially through government agencies and receive standard fees from incubatees. In a South African context, the main sponsors for incubators are SEDA Technology Programme (STP) and Incubation Support Programme (ISP) through the Department of Trade and Industry (DTI).

Unlike public business incubators, private BIs do not normally get sponsorships and funds from public funding. In this case, private BIs may have to depend on their own funds and sponsorship. According to Lalkaka and Shaffer [32], the main sponsor needs to “buy into” the business incubator’s mission and objectives, by assessing the performance, purpose, and idea behind the goal, and overall

incubator strategy. As business incubators increase both in developed and developing countries, the next generation of incubators are expected to be profit driven organizations that specialize in a specific sector environment [6]. This researcher also states that the idea of a profit driven incubator hinges on the perception of market failure and the associated difficulties that entrepreneurial venture face in obtaining funding from sponsors.

#### **4. Research Methodology**

This study adopted a qualitative approach to collect data by way of structured and unstructured interviews to gain in-depth knowledge and understanding of the challenges and prospect of business incubators in developing SMEs. A qualitative research method entails determining unanticipated findings without depending on numerical measurements and produces descriptive data obtained from interviews, questionnaires, and participant observation, in order to understand and describe specific social phenomena [34].

##### *4.1. Population*

The population comprises everyone who shares those characteristics defined by the researcher as relevant to the investigation [35]. Furthermore, the population refers to a subgroup of individuals relevant to the study. The research participants for this study were limited to business incubators who were registered on the database of Traction during the investigation. Traction is a company based in Cape Town that promotes SMEs development strategy and programmes. According to Traction's database, only five business incubators were within the Cape Town Metropolitan area. All five business incubators were deemed suitable for the study as they were within the locus of the study.

The sample for this study was drawn from the list of business incubators on Traction's database. Given that there are only five business incubators on traction's database, all of them were drawn for interview, and the respondents were business incubation managers.

##### *4.2. Data Collection and Analysis*

In this research, a qualitative method was used to collect data and content analysis was applied. The researcher was using structured and unstructured in-depth interviews, which were carried out in person with the respondents of business incubators in the Cape Metropolitan area. Therefore, the researcher utilised primary data. According to Skaik [36], primary sources consist of in-depth interviews conducted to gather first-hand information. Furthermore, the method of analysis applied coding with keywords coded into major themes and categories.

For the purpose of this study, personal interviews were conducted with five business incubator managers, and the study was done over a period of sixteen weeks. The incubators include Incubation Centres (ICs); Business Innovation Centres (BICs); Corporate Private Incubators (CPIs) and Independent Private Incubators (IPIs). The data collected from this study were analysed by means of content analysis.

## 5. Results and Discussion

### 5.1. Challenges of Business Incubators

The sub themes below are interpreted to address the research question of what the challenges are that are faced by business incubators in the Western Cape Province, South Africa.

### 5.2. Client Acquisition and SMEs Enrolled

These results, report on the number of SMEs enrolled in the incubation programme and those who have graduated. Drawing from the respondents' responses, an average 25 of entrepreneurs both graduated and were in the graduation phase. This sub theme set out to ascertain the number of SMEs that have graduated from the incubation programme. Akcomak [6] recommended that business incubators should set out a clear selection, entry, and exit criteria for the success of the incubator. Hence, as much as the development of the business incubator is dependent on the quality of entrepreneurs enrolled, it is important to have the incubates in the incubation programme for a specific duration and BIs should take a calculated risk to succeed [37]. The manager of Incubator 2 said:

“We currently have 28 incubatees in the programme. Only 18 of them are active, and we have not been really looking at graduating yet... We just provide them with office space and necessary skills for now. We believe that our clients have the qualities to grow their businesses. No one has left the incubation programme yet”. Therefore, this quote indicates the number of incubates on the programme and those who have left the programme.

Another respondent (Incubator 3) said:

“...Our goal is that 50% of the SMEs coming to our programme must become sustainable when they leave. Our output rate is also slower based on whether the clients stay or not. In the last 19 months that I have been here, I have graduated 1 incubatee out of the programme and that incubatee is successful and sustainable. The 50% target we strive to uphold is benchmarked against the world's average and at the moment the world average is 38%”. Therefore, this quote illustrates the importance of self-sufficiency and sustainability for BIs.

### 5.3. Challenges Faced in Running the Incubator

In reviewing the literature, data were found on the challenges facing incubators just like any other business [22]. In both developed and developing countries, incubators face obstacles that prevent them from fully contributing to the success of the incubated SMEs [24]. Drawing from the interviews, one of the business incubators faced the challenge of space to do production, funding, maintenance of machines, and technical and entrepreneurial skills. The results noted here, corroborate the findings of [13]. Emphasizing the challenges facing incubators, Incubator 1 said:

“...Our major challenge is the expansion to different areas, given that it is costly to setup up a new site and people might not participate”. Therefore, this quote indicates the challenges that are faced by incubators such as expansion to different areas.



Another interviewee (Incubator 2) said:

“Apart from getting our client’s mind-set right, our biggest challenge is on opening doors and connecting these entrepreneurs with corporate businesses. Furthermore, we have to make sure that the incubatees offer high quality products or services. Lastly, the challenge this incubator had at first was that the previous manager had no experience running a business before, neither was she an entrepreneurial person...there were operation systems that were not working such as, quality process systems, procedures were compromised”. Therefore, this quote illustrates the importance of having experience to manage an incubator with entrepreneurial attributes.

Therefore, the aim of this sub theme was to determine the challenges faced by business incubator in the Western Cape Province.

#### 5.4. Support Structures

Nowak and Grantham [38] argue that for-profit compared to not-for-profit incubators are expected to develop approximately half the overall number of all business incubators in the coming years. The main aim of this sub theme was to investigate whether incubators receive any kind of support from private and public companies. Drawing from the literature, one of the challenges facing business incubators was funding and support systems. The results illustrate that all of the respondents receive support of some sort from government institutions, while two of the participants indicated that they have not received any support from the private institution. The findings of the current study are consistent with those of Akcomak [6] who found that in developing countries business incubator are mostly supported by government agencies and there has been no transparency on the amount of funds that are allocated to business incubators.

Incubator 2 said:

“...Yes, we do receive funding from a government agency, 80% SEDA funding and 20% City of Cape Town. This is a very risky model; I am planning to change that model, to be funded up to 60%–40% by government, 40%–60% by private business”. Therefore, this quote indicates that this incubator is depending on funding from a government agent.

Another participant (Incubator 4) said:

“Yes, we have a number of private companies that support the incubator. The support is not limited to donations and finances... For this incubator, it costs R22, 000 per month to support an incubated business, and without the financial support they would not be able to pay themselves neither would we be able to accommodate them”. Therefore, this quote indicates that this incubator is receiving assistance from public and private companies.

#### 5.5. Self-Sufficiency

The results indicated that a majority (three) of the business incubators in the sample mentioned that they are dependent on government funding and they were not self-sufficient, while two incubators indicated that they were not reliant on government funding to be sustainable. This finding confirms the

association between [39] and [6] who concluded that business incubators should not depend on public funding, and it must develop a model that will lead to being self-sustainable. Encouraging self-sufficiency and sustainability, Incubator 5 noted:

“...We are an accredited training centre. Yes, we have a number of public companies that support the incubator. Funding to the incubation programme”. Therefore, this indicates that incubators in the Western Cape Province are not self-sufficient.

Another interviewee (Incubator 3) said:

“I think it’s a yes. Our model allows us to be sustainable; it covers our basics and at the end of the day we have to pay out facilitators and employee; but we get support and this makes life easy for us”. However, this quote illustrates the importance of government funding in maintaining the sustainability of an incubator.

The aim of this sub theme was to find out whether the business incubation managers who participated had a model that would lead to self-sufficiency.

#### 5.6. *Advanced Technological Facility (Prototype)*

The results illustrate that a majority of the respondents (60%) acknowledged that gaining access to technology-based facilities was not a major challenge, while only two (40%) indicated that lack of access to an advanced technology facility was a significant challenge that moderates their ability to provide efficient and reliable services to clients (SMEs). However, in developed countries, technological based business incubators are drivers of entrepreneurship, economic growth, innovation and R&D [40]. The results of this study will now be compared to the findings of Buys and Mbewana [37] who found that access to technological facilities and technical knowledge lead to a conducive environment for business incubators.

Drawing from the interviews, Incubator 1 said:

“...Not necessary, but yes to high tech facilities. We have facilities, but not upgraded facilities, we don’t need a lot of technology, we need access to the internet, platforms and we do have it and we buy it”. Therefore, this indicates the major challenge of a lack of advanced technological facilities.

Another respondent (Incubator 2) said:

“... The challenge is that people don’t know where to go. Hence, it is the role of the business incubator to know where SMEs should access these services. An incubator needs to have a credible knowledge of the industry”. However, this quote illustrates the lack of technological facility is not a major challenge among other incubators.

#### 5.7. *Relevance of Entrepreneurial Skills*

The results of this sub theme will now be compared to the findings of previous sub themes. There is a strong relationship between [6] and [7] who argue that business incubators in developing countries lack the managerial and entrepreneurial skills to fully contribute to the success of SMEs. The majority

of business incubation managers interviewed concurred that lack of entrepreneurial skills, inhibited their ability to successfully nurture incubated SMEs successfully. In contrast, two of the business incubation managers indicated that it is not a necessity to have entrepreneurial skills and that the formal qualification to run an incubator incubation managers need is to have passion and persistence in developing incubated SMEs. These results tend to corroborate the findings of a number of previous works in this field. Drawing from the participants' emphasis on the relevance of entrepreneurial skills, Incubator 2 related the following:

“...As much as entrepreneurs should have entrepreneurial skills and an entrepreneurship background to develop their businesses, incubation management are required to at least have an understanding of what these entrepreneurs are going through”. Therefore, this quote illustrates the importance of entrepreneurial skills in SMEs self-sufficiency.

Furthermore, it was found that the majority of the interviewees had formal qualifications, and some came from entrepreneurial backgrounds. It was also noticed that both incubated SMEs and the organizations that support them should have an entrepreneurial mind-set. It is therefore vital to promote a growth mind-set amongst entrepreneurs in the SME sector in South Africa as a means to foster SMEs success [41]”. Another interviewee (Incubator 2) said:

“I am currently rebuilding a model of the variety of skills to be mentored in the management department like human resource, finance, marketing, *etc.*” Therefore, this quote shows the importance of multiple skills to be provided to the incubatees.

## 6. Conclusions and Future Research

As South Africa joins the bandwagon in establishing business incubators as a means of supporting SMEs, it is important to note that these entities are as good as what they can do for themselves and their clients (SMEs). Thus, by examining and addressing the needs and sustainability challenges of business incubators, policy makers and other stakeholders would be promoting both business incubators and the relevant SMEs.

This paper investigated the challenges faced by business incubators (BIs) as they strive to support their clients. The study revealed that besides the desire to be self-sufficient, business incubators faced other challenges not limited to the lack of sponsorship, production space, advanced technological facilities and expansion into different areas which were found to be the major challenges faced by business incubators.

These researchers propose that future research could look into developing an effective business framework for incubators or look at the effectiveness of the incubation programme in developing incubated SMEs.

### Author Contributions

Thobekani Lose designed and performed the study, reviewed the literature and conducted the interviews. Robertson Tengeh assisted in fine-tuning the literature and results. All the authors contributed immensely to the conceptualization and development of the paper. Both authors have read and approved the final manuscript.

## Conflicts of Interest

The authors declare no conflict of interest.

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