DEVELOPING AN INCUBATION STRATEGY FOR OUDTSHOORN

by

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DECLARATION

In accordance with Rule G4.6.3, I hereby declare that the above mentioned treatise is my own work and that it has not previously been submitted for assessment to another university or for another qualification.

SIGNATURE:

DATE: 27 January 2011
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ABSTRACT

Business incubators, as recognised in their contemporary form, have a history dating back to the 1970s in the United Kingdom and the USA. South Africa is no stranger to this concept of business incubation either: Since the 1980s the Small Business Development Corporation (SBDC) operated business “hives” as clusters of small enterprises.

Business incubators are support facilities that empower and stimulate small-entrepreneurial businesses – from the financially vulnerable start-up period, until the time that the fledgling company is ready to operate more autonomously. Business incubators provide, as part of their services, affordable space, financial-management services, sound business advice and other development services.

Incubation stimulates the development of small-entrepreneurial businesses and, to this end, helps stimulate the economy. Thus, for South Africa to invest in the development of small growing businesses, is to invest directly in its larger economy and to address its own development challenges like employment-creation, income-generation and the alleviation of poverty.

It is in this context that this study discusses the development challenges of one of the rural areas in South Africa, Oudtshoorn, and aims to provide a viable strategy of business incubation for this area, in anticipation that in future lessons can be drawn from this and applied to other rural areas.

Oudtshoorn is a town in the Klein Karoo, in the Western Cape Province of South Africa. The strongest sectors in Oudtshoorn’s economy are agriculture and tourism. These two sectors should provide the basis for an empowering business incubator to strengthen and enhance smaller businesses in the town.

The study focuses on
• the development challenges of South Africa and, in particular, a rural town such as Oudtshoorn,
• the importance of investing in small entrepreneurial businesses so as to strengthen the country’s economy.
• the nature an significance of a business-incubation strategy for the Oudtshoorn area.

Background literature on South Africa’s development challenges was collated as well as information gathered on small-business support and incubation in particular. Literature was retrieved from local institutions as well as national and international sources. Case studies of incubators in South Africa and in other countries were included to enhance the understanding of the importance of business incubation. In addition, the researcher’s close networks with the Oudtshoorn municipality, the local Red Door office and the different role-players in the small-business support sphere allowed for an in-depth assessment of support for such an incubation project and the critical obstacles it may encounter en route.
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CHAPTER 1
INTRODUCTION AND BACKGROUND

1.1 Oudtshoorn’s Development Challenges

According to O’Neill, Terblanche & Keyter (1999: 7), the creation and expansion of small enterprises is one of the primary sources of new employment opportunities. Thus the establishment of new and successful enterprises is one of the keys to economic growth. Globally, the small-business sector creates more jobs than big businesses (Smit, 2004: 12). By inference, developing small businesses can present an appropriate vehicle for poverty relief, socio-economic empowerment and a means of strengthening global competitiveness. However, these small businesses encounter numerous problems in the early phase of their development.

South Africa faces major challenges in the spheres of employment creation, income generation and the alleviation of poverty. These challenges exist with varying degrees of intensity in both urban and rural areas of the country. In approaching these challenges, the small-business sector and its ability to create jobs, generate income and help modernise the economy, is generally viewed as critical. As is the case with the challenges identified earlier, the structure and dynamics of small enterprises also differ—between larger and smaller towns. If the role of the small-business sector is to be strengthened, it is imperative that the nature and growth potential of the particular region be carefully examined.

It is against this background that the topic of this study, small-business support in Oudtshoorn, should be viewed. Additionally, the focus of the study is further narrowed to one particular “tool” in the process of small-enterprise support, viz. the establishment of local small-enterprise incubators. The choice of the topic has been influenced by the fact that the researcher is resident in Oudtshoorn and is professionally involved in the SMME-support field, working closely with the local Red Door office.
In Oudtshoorn, as in many towns in South Africa, the small-business sector has enjoyed government support, in particular since 1994. Since the advent of the new local government, Oudtshoorn municipality has experienced an evolution of the local economic development (LED) thrust, giving more attention to SMMEs. In 2005 a Red Door office was established in Oudtshoorn to help meet the needs of small businesses. As a service provider for Red Door, the researcher is aware of the challenges faced by these small businesses. A business incubation strategy is therefore proposed as it could provide a much stronger base to address the problems encountered by small enterprises.

1.2 Focus on Incubators

A business-incubation strategy that supports and promotes small-business development could contribute to the government’s job and wealth-creation efforts. The objective of this research is therefore to contribute to small-business development in Oudtshoorn. The rationale for the provision of business-assistance services by business incubators stems from the fact that the majority of start-up businesses do not have all of the necessary resources and critical success factors needed for business success. Consequently, they struggle with a number of significant problems during the early stage of their business development. Many of these problems are compounded by insufficient initial capital and a lack of access to technical assistance and market information. In this regard the provision of incubator services might assist these firms to overcome such entrepreneurial constraints. Essentially business incubators provide convenient tenancies, in-house business services and advice and the opportunity to build links with kindred business operators (Schaper and Volery, 2004: 237).

During the last decade, the establishment of small-business incubators and other ways to cluster small enterprises in emerging settlements has attracted increasing attention: this includes developed countries as well as underdeveloped countries of Africa. It equally includes South Africa where the “small-business hive” – strategy of the former Small Business Development Corporation
(now Business Partners) – has made way for different incubator initiatives supported by Seda, local authorities and central government.

Thus the purpose of this study is to illustrate that a business-incubation strategy for Oudtshoorn is an enterprise-development strategy, aimed at accelerating the process of formation, development and growth of small enterprises by providing a range of business assistance including physical facilities, business coaching and networking.

1.3 The Research Problem

There is currently a lack of support structures for small-business development in Oudtshoorn. In cases where this support does exist, the ability of small businesses to access them is limited due to bureaucratic bottlenecks. This situation impairs local economic-development efforts and aggravated the social problems mentioned earlier. This research problem can therefore be stated as follows.

What type of incubator will be suitable for Oudtshoorn, and which strategy should be followed to effectively assist local small businesses to build successful enterprises through the functions of such incubator?

1.4 Research Methodology

The central part of the research is the exploration of a local strategy to establish small-business incubators in Oudtshoorn. To achieve this, certain background information had to be collated and interpreted. This section relied primarily on secondary data obtained from local institutions and national data sources.

The background information also includes a review of the literature on incubators as tools for small-business support. Apart from standard international literature, it includes coverage of South Africa’s best practice in this field as revealed from secondary data. The framework developed for Oudtshoorn’s incubator strategy is based on the background information mentioned above as well as
• case studies of incubators elsewhere in South Africa,
• case studies of incubators in other countries.

In addition, the researcher’s close networks with the municipality, the local Red Door office and the different role-players in the SMME-support sphere allowed a continuous assessment of support for such a project and critical obstacles en route.

Ideally, the material collated for this study and the conclusions drawn in the proposed strategies could be of value in the design of incubator-strategies for other regions. In this context it should be mentioned that the Eden District Municipality has been engaged in a broader review of an incubator strategy for the whole district, i.e. the major towns such as George, Knysna, Oudtshoorn and Mossel Bay.

1.5 Structure of the Report

• Chapter two describes the impact of the small-business sector on the economic development of Oudtshoorn,

• chapter three discusses the problems and challenges faced by small businesses in Oudtshoorn,

• chapter four provides a theoretical perspective of an incubator strategy within the context of small-business development,

• chapter five proposes an incubator initiative for Oudtshoorn to address the problems and challenges faced by small businesses with the support services and infrastructure that the incubator can provide,

• chapter six provides a summary and conclusion of the research findings.
CHAPTER 2

SMALL BUSINESS IN OUDTSHOORN’S ECONOMIC DEVELOPMENT

2.1 Introduction: Oudtshoorn in the Southern Cape

This chapter highlights the economic profile of Oudtshoorn as well as the role of different stakeholders with regard to the development of small businesses in Oudtshoorn.

Oudtshoorn is the largest town in the Klein Karoo and offers all the amenities of a regional capital – with all the charm of a traditional plattelandse dorp (rural town). The town services the agricultural industries of the Klein Karoo and is the site of the famous annual arts festival, the Absa Klein Karoo Nasionale Kunstefees (KKNK). It is known particularly for its ostrich farming and significant contribution is made by its tourism sector, with the Cango Caves, amongst other attractions, a world famous tourist destination.

2.2 Economic Profile and Sector Structure

The economy of Oudtshoorn relies mainly on the agriculture and tourism sectors, given the town’s location, its major attractions and the natural environment. The agricultural sector, with the ostrich industry’s Klein Karoo International (KKI) as the leader, is the biggest employer in Oudtshoorn.

Key activities in this diversified sector include the following.

- The ostrich leather industry, which was established in 1970, offers more than 160 direct jobs.

- Ostrich feathers are used to make fashion accessories such as boas, stoles and shawls. Factories for feather sorting and processing also contribute to approximately 300 direct and 400 indirect job opportunities.

- The three ostrich abattoirs contribute to more than 300 job opportunities.
• Seed production is another important economic activity, with Oudtshoorn supplying between 50 and 60 per cent of South Africa’s seed requirements (http://www.kleinkaroo.com).

• An olive factory, Olea, also contributes modestly to job opportunities.

• Currently active wine production activities include approximately 60 wine growers.

The other sector, tourism, also includes an array of activities
• The Cango caves, the largest show cave in Africa, attracts thousands of visitors, both locally and from foreign countries.

• The KKNK, South Africa’s biggest arts festival, has stimulated a wide range of activities.

• Endurance races, like the Cango Marathon, are held where participants qualify for the world famous Two Oceans and Comrades marathons.

• The “Hell and Back” mountain bike race (http://www.oudtshoorn.com), and other ad hoc tours also take place under the banner of the tourism sector.

Figure 1 and Table 1 show the relative size of all the sectors of Oudtshoorn’s economy for 2001 and 2007. The wholesale and retail trade as well as the catering and accommodation sector (which includes a part of the tourism sector) account for 22,7 per cent of the GDP in 2007, which is 2,6 per cent higher than in 2001. The sector for community, social and other personal services (24% of the GDP in 2007) mainly includes municipal and government institutions, the likes of social services, police, etc. It slightly decreased, similar to the sectors of agriculture and manufacturing in the Oudtshoorn area. The aforementioned sectors – agriculture and manufacturing – both relate primarily to the processing of agricultural products, signifying that agriculture and manufacturing should actually be combined, thus indicating the relative importance of agriculture-related activities (i.e. about 20% of the local GDP). One could apply the same logic to tourism and the hospitality industry, of which the activities are included in the respective sectors of trade, transport and finance. The total contribution of this sector to the Oudtshoorn economy could in all probability amount to 20 per cent as well.
Economic growth should not only be determined by the formal economy but also by the informal economy. In many cases the informal economy interacts with the formal economy by supplying certain goods and services. The linkages between the formal and informal sectors of the economy need to be understood and considered in devising a local economic development strategy. In the case of Oudtshoorn, informal activities are significant in both the agricultural sector and tourism.

TABLE 1: GDPR value of economic sectors at 2000 prices

<table>
<thead>
<tr>
<th>Sectors</th>
<th>GDPR-2001 (R’000)</th>
<th>GDPR-2007 (R’000)</th>
<th>Average Annual Growth Rate 2001-2007 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture, forestry and fishing</td>
<td>83 521</td>
<td>89 167</td>
<td>1.10</td>
</tr>
<tr>
<td>Mining</td>
<td>309</td>
<td>333</td>
<td>1.24</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>123 951</td>
<td>138 331</td>
<td>1.85</td>
</tr>
<tr>
<td>Electricity and water</td>
<td>58 822</td>
<td>57 951</td>
<td>-0.25</td>
</tr>
<tr>
<td>Construction</td>
<td>22 666</td>
<td>49 921</td>
<td>14.06</td>
</tr>
<tr>
<td>Wholesale and retail trade; catering and accommodation</td>
<td>192 836</td>
<td>268 617</td>
<td>5.68</td>
</tr>
<tr>
<td>Transport and communication</td>
<td>68 699</td>
<td>93 549</td>
<td>5.28</td>
</tr>
<tr>
<td>Finance and business services</td>
<td>150 579</td>
<td>198 166</td>
<td>4.68</td>
</tr>
<tr>
<td>Community, social and other personal services</td>
<td>256 270</td>
<td>289 391</td>
<td>2.05</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>957 654</strong></td>
<td><strong>1 185 427</strong></td>
<td><strong>3.62</strong></td>
</tr>
</tbody>
</table>

Source: Quateric

If the relatively large share of community, social and personal services is considered, it should be borne in mind that Oudtshoorn is an important educational centre (in the
Klein Karoo) and is located centrally in this region. It also provides a diversity of health and social-care facilities to other regions. Here again, the significance of small and medium enterprises as service suppliers should not be underrated.

### 2.3 Population and Employment

The population of Oudtshoorn is currently estimated at 79 604. Oudtshoorn covers 3 539 km$^2$, which translates to a very low density of 22,5 people per square kilometre (Economic Profile: 2008).

As shown in Figure 2, Oudtshoorn has the third largest population in the Eden District, surpassed by George and Mossel Bay.

**FIGURE 2:** Population of municipalities in the Eden District

![Population of municipalities in the Eden District](image)

*Source: Stats SA, Census 2001 and Community Survey 2007*

**TABLE 2:** Oudtshoorn’s population groups, 2001 and 2007

<table>
<thead>
<tr>
<th>Population group</th>
<th>2001</th>
<th>2007</th>
<th>Average annual growth rate 2001 - 2007 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Black</td>
<td>6 793</td>
<td>6 963</td>
<td>0.4</td>
</tr>
<tr>
<td>Coloured</td>
<td>64 763</td>
<td>60 703</td>
<td>-1.1</td>
</tr>
<tr>
<td>Indian or Asian</td>
<td>87</td>
<td>476</td>
<td>32.7</td>
</tr>
<tr>
<td>White</td>
<td>13 050</td>
<td>11 462</td>
<td>-2.1</td>
</tr>
</tbody>
</table>

*Source: Stats SA, Census 2001 and Community Survey 2007*

Table 2 above shows the four population groups, with the coloured group undoubtedly the largest group in Oudtshoorn.
Oudtshoorn’s employment pattern follows the sector structure. Thus, community, social and personal services constitute the largest share of formal employment, followed by trade and tourism, manufacturing and construction. Agricultural employment is low since much of the farming activities are outside the urban areas. Moreover, in agriculture, as in several of the other sectors, there is a significant component of informal (unregistered) employment and (subsistence) self-employment. In actuality, this fact complicates the identification of clear employment trends, since informal activities probably absorb in excess of 20 to 25 per cent of local labour inputs.

As indicated earlier there are a few larger employers in Oudtshoorn, but the overall pattern of employment is shaped by medium, small and micro-enterprises. As far as the longer-run trends are concerned, local employment is stagnant – not declining – which creates a challenge for the local economy. This challenge is further exacerbated by some migratory influx of Eastern Cape residents in search of employment opportunities en route to the Western Cape.

This employment challenge facing Oudtshoorn should be viewed as one of the reasons for a local incubator initiative.

2.4 Spatial Spread of Businesses and Settlement Patterns

Oudtshoorn municipality covers the town of Oudtshoorn, which includes the suburbs of Bridgton (formerly the main coloured township) and Bongolethu (formerly the African township) and also the smaller villages of De Rust and Dysselsdorp, both of which are classified as third-order nodes.
Map of Oudtshoorn
Oudtshoorn

Oudtshoorn is easily accessible by road from the Eastern and Western Cape. The town is strategically located at the nodal intersection of a number of major routes: to Prince Albert and the N1 route, along the N12 to Beaufort West in the north and to the coastal region and George in the south, along the N9 to Uniondale and the Eastern Cape in the east, along the R328 to Mossel Bay in the south-west, and at the start of the very popular R62 tourism route to Calitzdorp and Worcester westwards. The town’s nodal position in relation to access routes contributes towards its functional role as a regional service centre, which is directly relevant for the incubator initiative.

Bridgton

Bridgton is the suburb where the majority of coloured people live. The suburb is situated three to six kilometres away from the town centre. There are two business centres in Bridgton which have the potential to expand. Home-stays in the coloured area is a unique type of tourism business, as international tourists want to experience and mingle with locals while enjoying home-cooked meals, laughter and the classical storytelling around a fire.

Bongulethu

Bongolethu is the suburb where the majority of black residents live. It is smaller than Bridgton and located even further away from central Oudtshoorn, with considerably less local business development. As far as tourism activities are concerned, Ma Betty’s traditional Xhosa cultural village is situated in the township. Transport is arranged from the local tourism office. Thando tours take tourists on a township tour. There are a number of other small businesses such as tourist-focused spaza shops, arts and craft projects (such as beaded products and feather dusters) and also the manufacturing of clay pots by local black women. Spaza shops play an important role as income generators.
Dysseldorp

Dysseldorp is situated between Oudtshoorn and De Rust on the R29 to Beaufort West and is 20 km away from the Oudtshoorn town centre. The Klein Karoo Group contributed to a community project which involves the extraction of liquorice from the liquorice plant. The establishment of this project resulted in four permanent and fifty temporary job opportunities (http://www.kleinkaroo.com).

The liquorice project is a small industrial hub, located approximately one kilometre from the main road. Apart from the liquorice project, the Klein Karoo Group also contributed to the feather sorting project, which saw to the provision of approximately 200 jobs. There are other economic activities in the town in addition to a fruit drying factory in the southern part of the town as well as the Kolping Training Centre. Dysseldorp is also known for agricultural activities which include the growing of vegetables and seed production (Economic profile: 2007).

De Rust

De Rust has become known as a tourist attraction with a unique character. Various craft and art exhibitions, coffee shops and guesthouses can be found along its main road. The coloured area of BlomNek is situated on the north side of the village with potential for small-business development if properly supported.

2.5 Role-players in the Local Economic Process

The local economic development of Oudtshoorn and its linked villages is shaped by the action, interaction and cooperation of all the relevant public and private-sector entities. These include the different levels of government, the business community and all civil-society actors as role-players. One can briefly comment on the function of these role-players, since their involvement in an incubator project would also be relevant.
2.5.1 Provincial government

The Micro Economic Development Strategy (MEDS) of the province of the Western Cape plays a vital role in promoting SMMEs. According to the MEDS Round 1 (Phase Two), the provincial government’s role in supporting small businesses should not be that of “main deliverer” of services, but rather to focus its attention on

- channelling information to local service providers, which is aimed at building awareness of the full range of services provided by the national government,
- supporting and leveraging private-sector support delivery and
- building public-private partnerships.

2.5.2 Eden District Municipality

The Eden District Municipality together with the Oudtshoorn Municipality is equally responsible to ensure that communities, especially the disadvantaged communities, have access to resources and services. It is the role of the district to help local municipalities with finances, facilities and capacity building in order to reach the people of the area. It can also contribute to savings by sharing resources with others. The Eden region has a strong and highly diversified local economy and is endowed with rich natural resources; in actuality, the Eden District contributes more than six per cent to the GDP in the Western Cape. Agriculture and tourism are the drivers of the district economy.

The growth pattern of Oudtshoorn Municipality is marginally lower than that of the Eden District, but corresponds to the trend observed in the district.
Figure 3 tracks the economic growth trends of Oudtshoorn in comparison to Eden Regional District’s growth rates for the period 2001 to 2007. Oudtshoorn’s economy grew at an average annual rate of 3.6 per cent over the period compared to the district’s average annual growth rate of 4.4 per cent.

2.5.3 Local government – Oudtshoorn Municipality

The major function of local government is to ensure that appropriate, user-friendly and fully functional infrastructure exists to promote business development in the local area. SMMEs require a positive business-enabling environment to deliver prosperity. Municipal government has a key role in creating such a favourable environment for business development and success. In this context, the maintenance and construction of infrastructure are funded mandates of local government.

By nature, local economic development is a partnership between the business sector, community interests and municipal government. An Integrated Development Plan (IDP) is the principal strategic plan with respect to planning, management and development in the area, including steps taken in the small-business support sphere.

In line with national thinking, the LED office of the Oudtshoorn Municipality was created in 2004 and proactive developments started in 2005. It is the task of the LED office to administer the Economic Development Fund which is linked to the municipal
capital budget. Within the LED strategy the funds are allocated to projects expected to contribute to sustainable growth (Oudtshoorn Economic Profile, 2005: 4). This could also be relevant for the incubator initiative.

Another role of local government is to facilitate interaction with the different stakeholder groups in the private sector and civil society. We can now turn to them.

2.5.4 Red Door

In 2005 the Red Door was established in Oudtshoorn due to the ever-present need to improve the support provided by government to small businesses. This was a provincial government initiative and was introduced by the Department of Economic Development. A wide range of constraints were identified. In recognition of these constraints an intervention was sought to address the development of SMMEs, which were seen as a vehicle to drive the economy.

The Red Door office in Oudtshoorn is seen as a “one-stop shop” providing information, business advice, referral to accredited service providers and information on business opportunities. The personnel of the Red Door are business advisors who capture a profile of each person who visits the centre, perform a diagnosis of their needs and develop a plan to address these needs. The plan includes provision of necessary information, referrals to accredited service providers, linking the business to opportunities for skills training and, where necessary, help in the search for finance. Essentially the Red Door plays a catalytic role in the evolution of a network of service providers. However, it is envisaged that the Red Door will also play a constructive role in managing the quality of services rendered by the external service provider (Orford and Wood, 2004:8).

2.5.5 Klein Karoo Agri Business Centre

The Klein Karoo Agri Business Centre (KKABC) was founded in 2004 in response to the national government’s integrated plan to fight poverty. The KKABC, Absa and the Landbank combined forces with organised agriculture (Agri Kleinkaroo) and accepted the challenge to enhance the quality of life of people living in the rural areas around Oudtshoorn. The aim was to create a structure to initiate and develop agriculture-
related businesses. During 2008 the KKABC, supported by KKI and the Klein Karoo Co-operative, shifted its focus to be more community-based (http://www.agricraft.co.za).

2.5.6 Greater Oudtshoorn Tourism (GOT)

This association represents all tourism-related businesses as well as the municipality. Oudtshoorn is an internationally recognised tourist destination with tourists converging in the town especially from European countries such as the Netherlands, Germany, England and other eastern European countries. Approximately 350 000 tourists visit the area annually. Major tourism icons include the Cango Caves, Cango Wildlife Ranch and the ostrich farms.

Oudtshoorn is known as the capital of South Africa's ostrich industry. The birds are farmed for their feathers, skin and lean meat, which is exported all over the world, while their eggs are used for decorative purposes. The town's prosperity is in part evidence of the good business these big-eyed birds have become.

Visitors to Oudtshoorn can tour a number of ostrich farms, particularly around Oudtshoorn, where tours are organised on a daily basis. They can experience how the birds are bred as well as the various ways in which ostrich products are fashioned and marketed across the globe.

2.5.7 Klein Karoo National Arts Festival (Absa KKNK)

The Absa KKNK is a tourism product which, as any other product, progresses through a product life cycle. Research has been done by the Institute for Tourism and Leisure Studies at the North-West University in order to give better clarity regarding the role of the festival in the local economy as well as in a broader tourism context. The research specifically attempts to determine the economic value of this festival for Oudtshoorn.

According to the research that was done in 2009, 87 per cent of respondents of enterprises agreed that the Oudtshoorn area benefits from the Absa KKNK, whereas only seven per cent of them disagreed and six per cent were uncertain. All
businesses, especially restaurants and accommodation facilities, benefit to a great extent from the Absa KKNK.

The number of visitors to the festival in 2009 was estimated at 44,934, while their spending amounted to R84.4 million. The spending by visitors is considered the largest single contributor to cash injections in the Oudtshoorn area.

Given the size of the annual festival, the KKNK administration has to be viewed as a major player in the local economic development process.

2.5.8 Oudtshoorn Business Chamber

The role of the Oudtshoorn Business Chamber is to promote and protect the interests of the local business sector as well as to network and negotiate on behalf of its members. Membership to the Oudtshoorn Business Chamber is open to all businesses that are compliant with the laws that govern business conduct in South Africa.

The membership statistics have grown over the past year with, however, a substantial drop in membership during 2008, followed by a distinct recovery in 2009.

The statistics are as follows.

<table>
<thead>
<tr>
<th>Year</th>
<th>Paid-up Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>132 paid-up members</td>
</tr>
<tr>
<td>2008</td>
<td>87 paid-up members</td>
</tr>
<tr>
<td>2009</td>
<td>147 paid-up members (up to the end of October)</td>
</tr>
</tbody>
</table>

The chamber should also be viewed as a very important partner in any incubator initiative.

2.5.9 Oudtshoorn Women in Business (OWIB)

Oudtshoorn Women in Business (OWIB) was established in 2005 to create a platform for women from disadvantaged communities.
Its objectives include

- to promote self-employment amongst women as opposed to dependency on government grants,
- to equip women with the necessary management skills to run their own businesses effectively and
- to form strategic partnerships with established business people and other role-players in the economy in order to facilitate the development of women in business.

Once again, one would hope to see OWIB as an active partner in any incubator initiative.

2.5.10 International role-players

The main international role-player that currently contributes to economic development in Oudtshoorn is Alphen aan den Rijn from the Netherlands.

The community of Alphen aan den Rijn in the Netherlands signed an agreement of co-operation with the community of Oudtshoorn in 2002. The purpose of the agreement was to strengthen contacts between this organisation and individuals of both towns to increase international awareness (Economic Profile: November 2005). Such contacts could lead to practical steps to learn from Dutch initiatives in the incubator sphere. Ideally, it might lead to Dutch donor-agency awareness about such an initiative, which might pave the way for some financial support or volunteer-service inputs.

2.6 Conclusion

The summary of Oudtshoorn’s economic-development characteristics has revealed it to be a fairly “normal”, medium-sized rural town, with some distinct attractions and a strategic location, but in general a slow development path. The small enterprise sector – ranging from informal activities to medium-sized enterprises – plays a central
role, since there are no large corporates, and public-sector agencies are also rather small. At the same time we noted a range of public, private and civil-society players in the local sphere, with some of them quite relevant for any incubator initiative.

Attention will now be given to the problems encountered by these small enterprises in the Oudtshoorn area and the need for more effective and broader-based support to local SMMEs.
CHAPTER 3
PROBLEMS AND CHALLENGES FACED BY SMMEs IN OUDTSHOORN

3.1 Introduction

Taking into account the high failure rate of small enterprises during the first phase of existence, it is critical to look at these challenges and see how an incubator initiative could help to address them.

In Oudtshoorn is a high formation rate of new enterprises due to the platform created by government’s LED strategy in collaboration with the Red Door and Seda. In contrast, there is also a high rate of stagnation of the newly formed enterprises. The main purpose of Red Door is to help businesses with registration and basic start-up processes. The challenges arise when businesses embark on the next phase, which should be to develop systems in order to manage their businesses successfully.

In many cases they need someone to “hold their hand” or to guide them on this path of growth. The majority of small businesses do not have all the necessary resources and knowledge needed for sustainable success. According to Scarborough and Zimmerer (2001: 25), they struggle with a number of critical problems during the early stages of developing their business.

In the context of this study it is thus necessary to explore and identify the causes of failure of small businesses in Oudtshoorn, bearing in mind that the provision of incubator services should assist small businesses to overcome these constraints (Abduh, D'Souza, Quazi and Burley 2007: 77).

3.2 Challenges

Within the black communities the challenges that emerging small businesses in Oudtshoorn experience are often due to their background, where their predecessors were marginalised and precluded by apartheid from ownership of property, businesses and the capacity to create wealth. In addition, there are many other
factors that constrain the integration and growth of new enterprises. We can briefly summarise the main factors.

3.2.1 Physical Needs and Facilities

The absence of basic infrastructure or lack of reliable services, such as electricity or telephones in townships, informal settlements and rural areas makes sustainable business activities impossible (Harrison, Todes and Watson 1997: 43). Physical needs and facilities are usually the most expensive resources a new business has to acquire. Many SMMEs suffer from poor infrastructure facilities around their locations or inadequate access to even basic facilities.

They also experience ICT-related challenges which include limited and costly access to telecom services, particularly the internet. The use of appropriate technology is one of the most important factors behind a successful SMME’s competitive advantage (Nieman et al. 2003: 33).

3.2.2 Skills Needs

The educational standards of existing entrepreneurs in Oudtshoorn are often low, thus undermining their ability to manage, adapt and compete. Moreover, as a result of the legacy of apartheid education, the majority of the population in general is neither socialised nor educated to become entrepreneurs, but rather trained to enter the labour market as employees.

According to Zimmerer and Scorborough (2002: 23) small-business managers need to have experience in the field they want to enter. They need to gain working knowledge of the physical operations of the business and sufficient conceptual ability. They also need the power to visualise, co-ordinate and integrate the various operations of the business into a synergistic whole. Thirdly, they need the skills to manage the people in the organisation and motivate them to higher levels of performance.
The impact of training programmes for business skills that have taken place since 1994 will be felt only in the long term. In the interim they need all the support available to fill this gap, with an incubator as a useful potential tool.

### 3.2.3 Access to Finance

The issue of improved access to finance and credit is of major concern. Despite the establishment of Khula and other public-sector efforts in this field, it is clear that there is still serious lack of financial support for emerging entrepreneurs in the area. The formal finance system in South Africa has been a reluctant partner in support of developing small enterprises. As a result the majority of small entrepreneurs still have to rely on personal savings, loans from family and friends or informal credit sources (Rogerson, C. M. 2000: 6) as basis for initial business finance.

As a result of this lack of access to capital, many small-business owners make the mistake of beginning their businesses on a “shoestring”. In fact, small-business owners often misjudge the financial requirements of entering the business arena. As a result, they start off undercapitalised and can never seem to catch up financially as their companies consume increasing amounts of cash to fuel their growth (Zimmerman and Scarborough, 2002: 24).

Low-interest loans are sometimes provided for equipment and material purchases, and employee training is on occasion available through special government arrangements with local FET colleges. However, there is more to incubation than these few special facilities.

Strategies are needed to obtain resources for both the incubated small businesses as well as to sustain the business incubation programme. It is one of the tasks of the incubation process to prepare small businesses for these difficulties, while also providing them with support to get access to financial resources. Within the context of SMME support, small-business owners should be

- made aware of all the financial institutions with offices in the areas and
should be made to realise the important role of business plans when contacting financial institutions.

### 3.2.4 Access to Markets

Next to lack of finance the lack of easy access to markets ranks highest among small businesses as an obstacle to the growth of their business. Real obstacles are often mixed with a lack of realism on the part of SMMEs as to the quality and competitiveness of their goods and services offered as well as the reality of tough competition in different markets. Quite often they tend to produce and offer services that do not have a ready market. A major cause for this constraint is that most of them do not give priority to marketing in their overall business approach (Nieman et al. 2003: 33).

Of critical importance in the opening of new market opportunities is the fostering of greater business linkages between large enterprises and emerging small enterprises. Drawing on the experience of industrial districts or clusters, linkage programmes between small enterprises are a potential basis for market-expansion efforts (Rogerson, 2000: 695).

The basic mission of any business is to develop and sell products and services that respond to market demand. The business incubator should contribute to this mission by sensitising and training small businesses in this respect and providing them with strategic and operational marketing support.

### 3.2.5 Entrepreneurial Leadership

After the start-up of a venture its growth usually requires a radically different style of management. It’s a given that if the behaviours, systems and processes that drive entrepreneurial practice are not in place, it will be hard for the enterprise to take root (Finweek, 2009: 30).

According to Bruwer and Cilliers (2000: 4/5) entrepreneurial leadership is characterised by the following behaviour.
• **Innovativeness**: A willingness to introduce newness and novelty through experimentation and creative processes.

• **Risk-taking**: Making decisions and taking action without certain knowledge of probable outcomes.

• **Proactiveness**: A forward-looking perspective characterised by the foresight to seize opportunities in anticipation of future demand.

• **Autonomy**: Independent action by an individual or team to bring forth a business concept or vision and carry it to completion.

• **Personal motivation**: Focusing on the individual as a happy and balanced person who interacts successfully with other people and thereby influences other people positively.

“Entrepreneurial thinking is not optional. It’s more than a buzzword – it’s a business strategy. In many respects entrepreneurship and innovation are not just about growth – they’re about survival” (Ernst & Young World Entrepreneur Awards November 2009). While it is certainly not easy to create or strengthen such entrepreneurship, it is a well-known fact that business clusters and incubators can play a significant role in activating the learning process.

### 3.2.6 Business Networking

Networking between business owners is an important precondition for successful business growth (Rogerson, 2000: 693). Business owners learn from each other and can provide mutual support both professionally and personally. These factors help new businesses to stay alive and prosper.

A strong inclusive network, created through a business incubator, will lead to stronger, more inclusive networks for the incubated small businesses. Therefore, the business incubator must plan and implement a network of partners and allies that can contribute to both the business incubation programme and the incubated small businesses, thereby enhancing the conditions for growth and competitiveness.
This brief overview of challenges facing small enterprises has only covered the more critical aspects. Many other obstacles, affecting operators in different sectors, could be mentioned. If we look at the actual or potential steps to address these challenges there are also numerous players, programmes and initiatives engaged in these areas. We can think of conventional financial institutions (some of whom have special small-enterprise-finance schemes), conventional training centres (like FET colleges or private training centres), municipal, district, provincial or national SMME-support programmes and the efforts of specific NGOs or civil-society institutions to address particular needs.

In the context of this study we want to stress – and indicate in later sections – that an incubator initiative of sufficient dimensions can at the same time address most of these challenges to some extent. The incubator does not supply the full answer – for example, it cannot out of its own mobilise the funds to meet the financial needs of individual enterprises –, but it can be a catalyst or facilitator in the process of addressing the challenges indicated earlier. This can now be further elaborated on.

3.3 Incubators as critical Tools for SMME Support

Business incubators are viewed by many experts in the SMME scene as dynamic tools for fostering new ventures with the macro-objective of economic development and job creation, where small businesses are often viewed as the engines of growth. Incubation is a vital component of an entrepreneurial infrastructure with the concept moving mainstream, creating increased interest among policy planners. In fact, business incubators have become popular instruments of small-business promotion. This popularity is usually based on perceived minimisation of costs or the quest to minimise costs, given that the cost of the physical space, maintenance, telephone and answering services, office staff, equipment and supplies are shared. In addition, the services of business consultants, trainers, accountants and other experts are often available to the incubator tenant at a fraction of the “go-it-alone” cost (Rogerson, 2000: 693).
In South Africa this new concept of incubation is promoted by the Western Cape government as part of its Micro-Economic Development Strategy as set out in the Strategy Programme of 2004. Business incubation is, however, not yet widely seen as an agent of innovation or a gate for development. For many people it is still a new concept, and there is still a lack of professional expertise to successfully start and manage incubators. Technical assistance in this regard is needed from the start-up of the incubator until it attains sustainability (Meds 2004).

Once established and effectively operational an incubator should enhance the capacity of the small-business sector in the following ways.

- Provide training opportunities and improve the human resource base for entrepreneurship.
- Assist with expanding the access of entrepreneurs to finance and credit.
- Augment an often weak infrastructural base.

At sectoral level there is the further need to address the specific obstacles of small enterprises in the particular sectors. In this regard, there is a need to shift from the supply side to a more demand-side orientation in policy support, in order to confront the question of inadequate market opportunities and to foster strong inter-enterprise networks of co-operation.

3.4 CONCLUSION

The advantages and utility of an incubation model undoubtedly outweigh the challenges faced by small businesses. Successful incubation is not easy and requires a long-term commitment from all stakeholders, who will inevitably have to overcome many challenges along the way. Incubation can be a solution to help these small businesses to develop and make life easier if these challenges can be addressed. With the necessary input from all role-players, success is achievable.

The best way to find a means to develop such a system is to identify all the role-players of economic development and investigate the contribution that they will be
able to make in order to create a successful incubation model. Ideally, a well organised incubator will have relevant information about existing or upcoming support programmes available via its general office or other communication channels to enhance the capacity of small businesses. Through close contact between the incubator staff and SMME tenants it should be possible for entrepreneurs to get significantly better advice about appropriate support programmes than information-seekers who visit Seda or Red Door (Thomas, 2009: 21).

An effective way of ensuring that a business incubator will produce results, is to plan the incubator with the intention and goal to stimulate existing and generate new small businesses. These will then be able to carve out a niche of structured clusters and strategic chains, thus overcoming barriers to the development of sustainable enterprises.
CHAPTER 4
INCUBATORS AS A TOOL FOR SMALL-BUSINESS SUPPORT

4.1 Introduction

The development of hives or incubators for a cluster of small enterprises has for decades been on the agenda of small-business agencies and government departments worldwide. Incubators were previously called “hives”: a concept paralleled to bees in their beehives, as it described a cluster of businesses that share interests working together. Although different categories of bees undertake different functions, they similarly work together for the benefit of the hive. Business incubators have gained significance the world over as effective tools for economic growth and development. Modern-day clusters copy the historic pattern by grouping start-up and early-stage SMMEs with similar interests in a particular geographic location and provide them with an array of business services and resources.

There are many definitions of what constitutes business incubators. Gillotti and Ziegelbauer (2006: 1) describe business incubators as facilities that provide small entrepreneurial businesses with affordable space, shared support and business-development services. They can help young businesses during their start-up period when financial vulnerability is often at its peak. While not a panacea for a community’s economic struggles, incubators can enhance and stimulate the capacity of small business.

A second definition comes from the National Business Incubator Association (NBIA), which defines a business incubator as an economic development tool designed to accelerate the growth and success of entrepreneurial companies through an array of business-support resources and services. Their main goal is to produce successful firms that are financially viable and freestanding when they leave the programme. These incubator “graduates” then create jobs and strengthen local as well as national economies (http://www.nbia.org/best).
Nieman, Hough and Niewenhuisen (2003: 169) describe business incubation as an innovative system of support designed to nurture start-up and early-stage enterprises in a managed workspace. Throughout the developing world, small, medium and micro-enterprise incubators are considered to be innovative instruments of developing and promoting competitive small firms. True competitiveness requires businesses that can establish strong positions in niche markets through innovative products and services. Such businesses in their start-up stage are good candidates for incubation systems.

### 4.2 Historical Roots of Incubators

According to Campbell and Allen (1987: 3) the earliest business incubators, in their modern form, appeared in the United Kingdom in 1972. They were initiated by the subdivision of older vacant buildings by architects into “working communities” of design-related firms with shared accommodations and services. These developments were collectively managed and set up to create an optimal working environment for individuals in these trades.

NBIA, the US membership association for business incubation, identifies the origins of incubators in New York. It has been suggested that the foundations of incubators emerged out of the growth of managed workspace and enterprise centres in the 1970s. The NBIA itself was founded in 1985, starting off with only 40 incubators, and by 1995 more than 600 incubators were identified. The organisation is committed to providing its more than 700 members worldwide with advice to develop and manage successful business incubators. The organisation, based in Athens, Ohio, offers information, referrals, networking, news alerts, research and information resources, and it sponsors annual conferences and training programmes. It also seeks to build awareness of business incubators as a valuable business tool, and to inform and educate leaders as well as potential supporters and investors of the benefits of incubation. According to a 1991 study conducted by the NBIA, more than 80 per cent of the small businesses launched inside business “incubators”, successfully graduated within an average of two to three years to stand on their own (http://www.nbia.org).
In the United States of America, three historical roots have been identified in the development of business incubators. The first began with efforts to redevelop inner-city blighted areas and it grew to include distressed areas throughout the Midwest and Northeast. The second started as an experiment funded by the National Science Foundation to foster entrepreneurship education, development of new technologies in existing companies as well as the establishment and nurturing of new businesses and innovations at major universities. The third arose from the initiatives of several successful individual entrepreneurs or groups of investors who sought to transfer their own new venture experiences to start-up companies through an environment conducive to successful technological innovation and commercialisation (Campbell and Allen, 1987: 80).

The historical development of incubators has already achieved a place in local economic development strategising as an element of entrepreneurial assistance. Consequently, new applications of this concept are becoming more refined and specialised. For example, some incubators are open only to technology-based companies, others are reserved only for minority groups, such as women or youth entrepreneurs.

According to Laura Reese from the Global Urban Studies Program of Michigan State University, an important historical root with regard to business incubators stemmed from efforts to enhance innovation and entrepreneurship through university-related incubators or innovation centres. Indeed, universities have always been a source for early innovations because of their freedom to choose research projects and the resources available to them. A case in point is the Republic of Korea, which has 300 technology incubators, most of them connected with the Korean government and in co-operation with universities and schools throughout the country (Richards, 2002). Research conducted by Campbell and Allen (1987) indicates that university incubators are more apt to attract research and development firms, while public facilities are more likely to have light manufacturing, and private facilities tend to have retail or services tenants.
Another difference between the various types of incubators is found in its rent-pricing structure which follows a very predictable pattern. Private facilities charge the highest fees, but with the fewest services included. Universities charge one-third less than their private counterparts and offer more services, while public incubators charge the lowest rent and provide nearly the same services as university-sponsored incubators. Employment growth is slightly higher in university incubators, followed by public and then private incubators. Highly rated in these incubators are the availability of business services, interaction with other firms and the supply of management services. For entrepreneurs located in university incubators, interaction with the university, of course, also rates as highly positive.

The use of business incubators as a development tool continued in the 1980s. Cities, local governments and non-profit organisations in stagnating or declining small towns and rural areas, started business incubators either on their own or in partnership with other local public and private organisations (Campbell and Allen, 1987; Rice and Matthews, 1995; Richards, 2002). Throughout the Northeast and Midwest of the USA, these incubators were spurred on by plant closures and high unemployment. The new incubators were often specifically targeted towards new labour-intensive enterprises (Campbell and Allen, 1987).

A number of studies have been conducted in Australia and other countries outside the USA to investigate the assistance services that business incubators offer to their clients. They all confirmed that incubators provide their clients with a wide range of assistance services, ranging from tangible (e.g. physical facilities, machinery and office equipment) to intangible services (such as emotional support) through direct counselling by incubator managers or mentors, as well as interaction with other clients and bridging networks to business people outside incubators.

### 4.3 South African Incubator Initiatives

The incubator concept also has an extensive history in South Africa, reaching back to the 1980s, when the Small Business Development Cooperation (SBDC) was started as a public-private partnership. Up to 1994, when the former SBDC was disbanded,
more than 50 smaller and larger “hives” were established across South Africa, including a successful one in George and smaller ones in Oudtshoorn, Knysna and Mossel Bay (Thomas, 2009: 52).

The following subsection examines this early South African phase of business hives. A number of other programmes, which have evolved since the new government initiated the White Paper on Small Business Development in 1994, will also be discussed.

Currently, South Africa’s incubation process is still in an evolving phase. The literature provides important insights into the nature and workings of business incubators to date.

4.3.1 SBDC Hives

During the reign of the Small Business Development Corporation, established in 1980, important trends with regard to small business incubators emerged.

- A few large hives were established, attaining much publicity and achieving major impact in areas like Pennyville near Soweto and Blackheath in Cape Town.
- Hive structures were gradually spread to more and more of the larger towns.
- A distinct dualism evolved between smaller hives which primarily provided premises (with little other support) and the relatively larger hives, which could afford full-time support staff for entrepreneurial development.
- There was increasing awareness about the marketing needs of hive tenants.
- There were constant battles about rentals, with weaker industrialists finding even the moderate rentals “unaffordable”, with the financially stronger tenants then demanding “equal treatment” (which suited them).
- There was wide-spread dissatisfaction among tenants that the SBDC was not doing enough to strengthen tenants as “developing industrialists”.
- With administrative and other support staff included, most of the hives could not break even, notwithstanding initial grant funding. On the basis of loan capital
obtained at market-related interest rates, virtually all hives of the SBDC were operating at a loss.

- Efforts to improve the financial viability of individual hive projects almost inevitably led to a curtailment of support staff (full-time hive managers, mentors, etc.) with the property-administration role usually left as the minimum activity of the SBDC (which again strengthened critical views about the SBDC “not contributing to development”).

- The SBDC’s most successful hives were located outside African townships, with the tenant mix including white, coloured, Indian and African tenants.

- Over the years there was a continuous tussle about the sale of hive units. Successful tenants were interested in long-term tenure, being fearful of rising rentals. Thus they were keen to buy their units. Others wanted to be more flexible, whereas most of the starters would in any case not be able to afford a realistic purchase price (which often did not stop them from demanding the sale (or rather “granting”) of units, in order to relieve them of the awkward rental obligation).

According to Thomas (1992: 13), the clustering of sector activities in the larger hives resulted in strong learning processes, whereas the opposite happened in the very small hives, where poorly motivated tenants benefited little from each other.

During the SBDC era that ended in 1994, nearly 50 small-business hives were developed across the country as infrastructure facilities to accommodate small enterprises in affordable premises, and offering a range of business-development services available on site. Many of these hives had a lasting positive effect on emerging and other enterprises. Those which had no support services showed mixed results, and a few were outright failures due to poor location, poor tenant selection or weak management. When the SBDC was transformed into Business Partners after 1994 the new (predominantly privately funded) company was not willing to take over these hives. In reality, the Department of Trade and Industry (DTI) took the hives over as part of the State’s capital in the SBDC.

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Unfortunately, the DTI did not actively pursue this hive programme, with some of them being privatised (i.e. the units being sold to tenants) and others let for the tenants to develop a new partnership. This was only successful in a few exceptional cases.

Thus, the main lesson from the SBDC hives phase was the need to have a reliable funder for any locally rooted incubator. This aspect will also be critical for the Oudtshoorn project.

4.3.2 Seda Incubators

As one of the more specialised types of “new-generation” incubators in the post-1995 era of South Africa, technology incubators have emerged as new forms of venture creation and instruments of SMME promotion. The state-owned Small Enterprise Development Agency (Seda) is the facilitating body for several of these new incubators. A brief look will be taken at the incubators and some general trends. The two examples are the Furntech and Acorn incubators.

- The *Furntech incubator programme* was established in 2000 as a partnership between the Department of Trade and Industry (DTI) and the Tibro Training Centre (TTC) in Sweden, through a bilateral agreement between the DTI and the Swedish Industrial Development Agency (Sida).

Furntech’s mission is to be a productivity-driven, globally competitive, outcomes-based training provider that offers comprehensive and innovative business incubation-services in order to assist in job- and wealth-creation in South Africa’s furniture and wood-products sector. Its objectives are to

- provide business-technology incubators for furniture and wood-products industries,
- develop business and production expertise through skills development and technology demonstration,
- establish centres of excellence in key locations nationally,
serve as a vehicle to enhance the ability of the wood-processing sector to become globally competitive.

The organisation’s Board of Trustees responded to the increasing demand for the organisation’s skills-development and business-technology incubation services by expanding its presence from initially one centre in George in the Southern Cape to centres in Cape Town, Johannesburg, Durban and Umzimkulu in kwaZulu-Natal, in White River in Mpumalanga and in Mthata in the Eastern Cape.

Furntech’s process has been enhanced by partnerships and linkages with tertiary-education institutions, including the Nelson Mandela Metropolitan University in George (NMMU), the University of Stellenbosch and the University of British Columbia in Canada.

Furntech’s partnership with the Swedish TTC ensures that the organisation benchmarks its facilitator skills to meet the needs of its stakeholders while developing the international competitiveness of all manufacturers in the sectors. In fact, Furntech has become the leading developer of a sustainable model for manufacturing incubation in the furniture and wood-product sector. Its reputation has extended beyond South Africa and the organisation has been invited to participate in incubation conferences in China, the USA and the UK.

The incubation process involves assisting selected entrepreneurs with all aspects in starting up and developing their company into a sustainable business, while reaching milestones within an agreed-upon period. This process promotes entrepreneurship and encourages the formation and development of sustainable registered small and micro-businesses. Furntech’s training and recognition of prior learning (RPL) policies are based on the Skills Development Act and the South African Qualifications Authority (SAQA) regulations. The main goal of these policies is to add value to the skills-development process so that both the employee and employer benefit. The value-adding process is based on the premise that the registered qualifications and unit standards specify minimum
standards to be achieved, while Furntech tries to exceed these standards, wherever possible.

All Furntech centres are accredited by the Forest Industries Education and Training Authority (FIETA) to offer learnership, skill programmes and short courses in the four disciplines of cabinet-making, wood-furnishing, wood-machinery and upholstery. Furntech’s technology-demonstration service to the industry tries to create awareness of new technologies that challenge current thinking and methodologies. These demonstrations are leading to enhanced understanding, knowledge and acceptance of new technologies, and to technology transfer and innovation (http://www.stp.org.za/centres/furntech.html).

- The second example, Acorn Technologies, is a biomedical, bio-engineering and biotechnology start-up business incubator based in Observatory, Cape Town. Acorn Technologies provides residential and laboratory facilities, business expertise and a supportive environment for entrepreneurs and fledgling life-science businesses. The vision of Acorn Technologies is to bridge the gap between product development and commercial enterprise in the life-science and biotechnology sectors. This is achieved by providing suitable start-up businesses and techno-entrepreneurs with a range of business resources, including the facilitation of access to finance and virtual incubation.

Acorn stimulates and helps to commercialise viable technologies through world-class service provision and value-adding in the following areas.

- Commercial and technical services
- Space and facilities
- Administrative services
- Education and marketing
- Business plans and models
- Financial modelling
Both Furntech and Acorn have been established to stimulate economic growth, particularly in the high-technology SMME sector. Initially, the technology stations programme was developed by the Department of Science and Technology to strengthen and accelerate the interaction between technikons and SMMEs. The specific activities of the technology stations include, *inter alia*, research, development and application of new technologies, technology transfer, troubleshooting, quality advisory service, product development, simulated production units, testing services and secondment of staff and students to the unit. Technikons or Universities of Technology are increasingly becoming responsive to the long-term needs of small firms. At the same time, the creation of new jobs in a knowledge-based economy can be seen as a decentralised process that can be carried out by small firms and local universities.

According to Thomas (1996: 3), the development of small businesses can be seen as our economic survival for the future, which calls for business incubators that foster the entrepreneurial spirit, encourage technology transfer and, through that process, stimulate job-creation and neighbourhood revitalisation. He stated that if South Africans are to compete in a global marketplace, the development of new and innovative businesses is critical.

Effective incubation enhances the successful development and growth of SMMEs by helping them survive during the start-up period when they are most vulnerable. Most incubators offer their clients office space and shared administrative services. Business incubators offer assistance with business basics, networking activities, marketing, business management and training as well as soft skills such as presentation skills and business etiquette.

### 4.4 Physical and virtual Incubators

Typically, a physical business incubator begins with a facility/building offering a common location for new firms. Public subsidies may allow below market rentals for prospective firms. In addition to lower rents and co-location with other, typically related, new businesses the incubator includes an array of support services designed
to meet the needs of small start-up firms often owned by inexperienced or first-time entrepreneurs. The most common operational form in North America is for incubators to be run by non-profit organisations: 90 per cent are structured in this manner. More specifically, 25 per cent are sponsored by academic institutions, 16 per cent by government entities, 15 per cent by economic development organisations and about 10 per cent by not-for-profit entities (http://www.nbia.org).

In sharp contrast to a physical incubator, the virtual model allows a company to gather advice of an incubator without actually being located at the incubator site. This model suits those entrepreneurs who need the advice and other support of an incubator, but still want to maintain their offices, warehouses etc. (http://www.en.wikipedia.org/wiki/virtualbusinessincubator).

A virtual incubator for that matter consists of four defining services:
- Entrepreneurial start-up support,
- office support,
- access to financial resources and
- access to networks.

Naturally, a virtual incubator is far more flexible and can therefore accommodate more small businesses than a physical incubator. However, the absence of a contiguous environment between the enterprises and the service suppliers complicates the process of reaching all the incubatees.

The advent of the internet age has ushered in a period of significant development of new models of doing business and managing organisations. Developments in information technology are in reality enabling, if not driving, enterprises to adopt new work practices, new organisational structures and even new management styles in order to extend their businesses both domestically and abroad.

According to Nowak and Grantham (2000: 130), successful models for work organisations in the “new economy” are epitomised by the virtual incubator and include small-scale networks of interlocked specialists converging on a temporary basis to approach a focused market or software project. For example, a combination
of relatively autonomous entities may stay together just long enough to meet its members’ specific goals and then disband, with individuals and teams moving on to other projects and other ventures.

For the purpose of a possible virtual incubator for Oudtshoorn, discussions between role-players regarding the concept and its feasibility need to take place with the prospect of linking firms through communication and other bonds into a virtual incubator. Ideally a local “project” should include both a physical base for an incubator and different virtual incubation initiatives.

4.5 Sector Focus of Incubators

Pertaining to the clustering of small enterprises in a location (i.e. a physical centre, an area in a town or village or at some central place), a great deal depends on the sectoral composition of the clustered enterprises. It may be an unstructured mix of firms or firms from a few predominantly closely related sectors – or it may be a preselected combination of enterprises within a particular supply chain. Thus, one might find an incubator filled with high-tech, research-focused enterprises in the medical field or in furniture and wood-processing. One might also find an incubator focusing on crafters adapted to a particular region or primarily attracting clothing producers, tailors and other firms related to the clothing industry.

In a small town, which has only a limited number of small enterprises, it may be most appropriate to leave the mix of firms in an incubator open – this is to ensure that all the units are occupied and the cluster is home to some dynamic firms. In larger places or at particular locations (for example near a large factory or a university), one might rather focus on a narrow range of interrelated firms who could benefit more directly from this proximity.

Viewed from the perspective of a town’s growth potential, it would seem logical to focus on the particular sector/s which can enhance that growth if one plans, establishes and expands an incubator. For instance, in an agricultural area where the processing of local agricultural products constitutes a significant growth potential, it
would seem appropriate to let the local incubator focus on agri-processing SMMEs. As a location close to some tourism attraction, it might be sensible to establish an incubator that clusters tourist-focused service suppliers, craft producers and related enterprises.

Yet, if local business leaders and the local authority wish to diversify business activities, an incubator could be the most appropriate tool to attract some firms in the new, more promising sector/s. Thus, a town with declining activities might use an incubator strategy to push local production into some new sub-sectors (like agri-processing, tourism or health services).

### 4.6 Services offered by Incubators

The provision of incubator services should be seen as a holistic mechanism to address the needs of start-up businesses. For the purpose of this study, incubator services can be classified into three main categories.

#### 4.6.1 Facilities-related services

Since rent is a major expense for fledgling enterprises, incubators usually provide clients with affordable and flexible space. Affordable means that rent is usually charged at a rate below market rents. Flexibility means that the size of space can be increased or decreased as clients’ needs change. It may even be arranged that incubatees or clients pay the rent in instalments spread over a period of time.

Services relating to building facilities should also include conference or meeting rooms, cafeteria and lunchrooms, building security and other amenities related to the physical infrastructure and real estate. Business incubators might also provide clients with shared office services and equipment that start-up ventures require but typically cannot afford or often neglect or ignore. The practice of resource-sharing may yield a synergistic cost advantage. Accordingly, by offering these basic office services, business incubators provide opportunities to reduce costs and save time for entrepreneurs who want to start their businesses immediately (Abduh et al. 2007: 77).
Other important services may include an enhancement of visibility and credibility of clients’ businesses by transferring to clients the credibility and visibility of the incubator through the use of its postal address, branding of the incubator and, more generally, positive word-of-mouth among business people within the incubator’s networks and contacts (Culp, 1996; Martin, 1997; Smilor and Gill, 1986).

4.6.2 Counselling- and business assistance-related services

Counselling or mentoring services cover a wide range of professional activities, including developing a business plan and offering support in strategic planning, helping with accounting and financial management and in other areas like sales or marketing advice, legal advice, education with respect to government regulations, product development and employment assistance.

Typical incubators may offer focused training or educational services such as short courses, seminars or workshops. Alternatively, the incubator staff may help tenants to find the most appropriate training programmes offered locally or via correspondence. Since capital is often a critical requirement at various stages of the business-development process, business incubators may also assist their clients to obtain relevant information about capital sources and how to get into contact with potential investors (Abduh et al., 2007: 77).

4.6.3 Access to internal and external networks

Admission to an incubator facility implies that the clients get access to the incubator network as an instrument to broaden access to information, transmit information between entrepreneurs, build markets, lower business costs and save time. By locating clients under one roof and providing them with common meeting facilities, cafeteria and the like, incubators create opportunities and an environment conducive for clients to interact and create synergy.

Markley and McNamara (1995: 2) identify the following services and advantages of an incubator in this context.
A shared facility to benefit from the assistance, services, networking opportunities and flexible below-market rental space.

Tangible benefits such as lower operating costs and access to services.

Intangible benefits such as moral support, advice from other tenants and access to information.

The incubation centre provides entrepreneurs with appropriate advice and counsel and serves as a “switching centre” to other people and resources, as needed.

Incubator programmes are housed in incubator centres in which companies can co-locate, rent space and share business services and equipment.

According to Audretch (2003: 171), firms within a cluster/incubator often perceive more clearly and rapidly new buyer needs and benefit from the concentration of firms with buyer knowledge and relationships.

### 4.7 Managing Incubators

In as far as an incubator is a project or programme to accommodate a significant number of new, emerging or expanding small enterprises through co-ordinated support, the central role of efficient management of that project or programme should be obvious. How is the need for such a project established? How are local demands and opportunities objectively assessed? Who are the critical role-players and how are they brought together? How is co-operation between the private sector, public authorities and NGOs activated? Who “manages” the development of the particular building (complex), and how are the different support programmes (which are needed or desirable) brought together? And, to crown it all: How is the funding of the incubator structured and how are public-sector support funds mobilised?

This long list of challenging, practical tasks indicates the wide range of “management activities” linked to an incubator programme. Experience all over the world (and the hive-experience of the SBDC) very clearly illustrates that the management task is
probably the biggest challenge of all incubator efforts. It is not the purpose of this brief subsection to detail all these management tasks – at any rate, a great deal of these tasks will vary widely between projects and locations. Nevertheless, in the next chapter, where the Oudtshoorn project is discussed, it is imperative to go in some detail into the management challenges likely to arise.

One of the most critical questions in this sphere relates to the ultimate ownership and control of the incubator. Is the project public-sector-driven and -owned, with ultimate managerial responsibility falling upon the municipality, or is it private-sector-driven, with an “incubator board” ultimately controlling the project? In line with contemporary thinking about public-private partnerships and social enterprises, we find a number of projects controlled by a board with mixed representation of public, private and civil-society interests. Once again, the particular mix should be influenced by local circumstances, weaknesses and strengths.

Closely linked to the management of an incubator programme is, of course, the funding of the structures and processes. This will be covered in the last subsection.

4.8 Funding Incubators

Managing an incubator’s finances is a challenging task. Incubators usually rely on a mix of revenue streams – including rent and other payments from tenants and income from sponsors. In a well functioning incubator, tenants will come and go; a feature which brings an uneven cash flow to the incubator itself and which therefore needs close monitoring, if the incubator is to cover its running costs.

As is the case with all enterprises, incubator finances consist of revenue and expense streams as well as start-up and expansion capital. Consequently, financial management consist of the planning, overseeing and controlling of the incubator funds, whether they are garnered through services or provided by partners and investors. Mechanisms need to be developed that allow the incubator manager to accurately know the amounts available, the needs and the investment capacity. In
addition, financial management should focus on bringing in new sources of funds for the incubator.

Table 3 provides a schematic summary of the different financial needs and potential funding sources of incubators. We distinguish three broad categories, viz. *start-up and expansion capital, running cost* of basic services, maintenance of facilities and the administration of programmes, and, thirdly, *funds needed for individual tenants or “incubatees”*. The “sources” column indicates a variety of sources, which include the following.

- Larger public-sector grants and/or regular running-cost subsidies (which could come from any level of government).
- Corporate grants or the “donation” (or rent-free use) of buildings and/or equipment.
- NGO grants and/or regular running cost subsidisation.
- The utilisation of regular NGO-funded SMME support services (e.g. information-office facilities, mentoring voucher schemes, training facilities, etc.).
- *Ad hoc*-funded special (sector-focused) support tailored to the incubator.
- Service charges and regular (monthly, quarterly, annual) fees payable by tenants.
- Foreign-aid programme finance.
- Volunteer support.
- Regular bank finance and other (micro-)finance facilities.
- Direct funding of external services by individual incubatees.

This wide range of potential funding sources once again stresses the importance of creative leadership and management of such projects: If all the potential funds and existing support programmes offered by public, NGO and private sources are effectively drawn upon, it should be possible to fund such initiatives. At the same time, experience in South Africa and other countries has shown that lack of funding all too often curtails the range of support facilities and services actually offered by an incubator.
### TABLE 3  Capital and revenue sources of incubators

<table>
<thead>
<tr>
<th>Type of Expenditure</th>
<th>Sources</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A  Start-up and expansion capital for the incubator</strong></td>
<td></td>
</tr>
<tr>
<td>1  Core incubator structure/s, including renovations/expansions</td>
<td>* Donation from municipality or corporate sponsor</td>
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<tr>
<td></td>
<td></td>
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<tr>
<td>2  Equipment for joint use</td>
<td>* Donation/public-sector grants, project loans (recovered via user fees)</td>
</tr>
<tr>
<td>3  Basic office facilities and equipment</td>
<td>* Donations</td>
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<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>B  Running cost (physical and virtual incubator)</strong></td>
<td></td>
</tr>
<tr>
<td>4  General facilities and administration (running cost)</td>
<td>* Ongoing project grant (e.g. from municipality or Seda)</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>5  In-house services to incubatees</td>
<td>* Ongoing project grants or special-programme funds</td>
</tr>
<tr>
<td>6  Utilisation of external support programmes</td>
<td>* Use of Seda, DTI and other programme services (including voucher schemes)</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>7  Mentoring of incubatees</td>
<td>* Use of national mentoring schemes</td>
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<td></td>
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<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>C  Enterprise finance</strong></td>
<td></td>
</tr>
<tr>
<td>8  Start-up capital</td>
<td>* Tenants’ own funds</td>
</tr>
<tr>
<td></td>
<td></td>
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<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>9  Working capital</td>
<td>* Regular private-sector finance</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>10 Expansion capital</td>
<td>* Private-sector finance, utilising available incentives and support</td>
</tr>
</tbody>
</table>
4.9 Conclusion

This chapter provided an overview of literature with relevance to incubators, with the aim of providing a conceptual framework for the Oudtshoorn case study. It focused on business incubation as a tool to accelerate the successful development of start-up and fledgling companies by providing entrepreneurs with an array of targeted resources and services.

The review has shown the large number and great diversity of issues relating to the initiation and development of physical as well as virtual incubators. It is these diverse issues which constitute the challenge for the Oudtshoorn community if and when they embark on a serious incubator initiative. Most of the issues will take time to evolve and be dealt with, but all of them need to be conscientiously addressed from the outset.

The next chapter will focus on the more critical steps and aspects of this process in the context of Oudtshoorn.
CHAPTER 5
AN INCUBATOR INITIATIVE IN OUDTSHOORN

5.1 Introduction

The success of any incubator initiative depends on the long-term commitment from all the role-players, who will inevitably have to overcome many challenges en route. The need to leverage the support of the public and private sector as well as the local community should be regarded as critical. In the context of Oudtshoorn, close partnership will be integral to the success of the establishment of the two proposed sectoral incubators, since it facilitates the leveraging of resources and harnessing of the knowledge and contact networks necessary to maximise the potential benefits of the incubation experience.

A major change in attitude towards small-business development in general and towards informal-sector businesses is needed. The public needs to learn and accept that businesses from the private and informal sectors can co-exist and be mutually beneficial. The private sector needs to realise that a viable informal sector can help them to expand and develop their businesses as their potential market will increase concurrently. Likewise, all the urban role-players in Oudtshoorn have to understand and accept the close urban-rural interaction in any development efforts.

A joint initiative of the municipality, the local community and business leaders can unite all economic forces in the local situation to identify resources, understand the needs and tailor plans in order to produce such an initiative.

This chapter emphasises the importance of public-private partnerships in creating successful incubators. It also addresses the contribution and responsibilities of each role-player whether it be funding, managing or sharing of expertise in the development of a local incubator in the Oudtshoorn area.
5.2 Sector Focus of Incubators

The second chapter of this research piece has made it evident that the two largest economic sectors in Oudtshoorn are the agricultural and tourism sectors. Both of these sectors have significant potential for small enterprises, both formal and informal. In the agricultural sphere urban agriculture as well as small farmers will be discussed. More important, however, are small firms supplying services for existing or emerging farmers in the area, small-scale food-processing enterprises as well as small traders and transporters active along the food-supply chain in the region.

In the tourism field we can distinguish three segments, viz.

- crafters and craft traders who want to service the needs of visiting tourists (at the Cango Caves, in Oudtshoorn and its townships as well as along the highways),
- direct suppliers of services to visitors, like accommodation, restaurants, etc.,
- suppliers of transport and other services to the tourism sector.

While the crafters and traders are usually the most visible segment of small enterprises in the tourism sector, more specialised service suppliers are also important and would in fact benefit greatly from the clustering of activities in an incubator area.

Thus, establishing two types of incubators could be the answer to accommodate small businesses from the two most promising sectors separately. Considering all the evidence discussed in previous chapters as well, Oudtshoorn has a comparative advantage as far as tourism and agriculture are concerned.

As part of its efforts to stimulate LED at the regional level, the Eden District Municipality has undertaken desktop research on the possible initiation and facilitation of a process to develop small-enterprise incubators across the Eden District. Initiating a business incubator for the tourism and agricultural sectors in Oudtshoorn would be a kick-start of the process for Eden’s district-wide strategy.

A business incubator focusing on these two sectors could pave the way for future incubators to accommodate other sectors as well. It implies providing an environment
that is conducive to SMME development in the framed sectors through the provision of effective support services such as training, mentoring, financial-management assistance and other aspects relevant to building sustainable tourism and agricultural businesses.

Such a sector-focused approach could also help local government to reach its targets in initiatives such as the Integrated Development Planning (IDP) and the Local Economic Development (LED) strategies. The incubator should also address other key issues like broad-based black economic empowerment (BBBEE).

Against this backdrop, the incubator strategy proposed for Oudtshoorn is not a blueprint but rather a broad strategy, subject to discussions and negotiations between all the relevant role-players.

5.3 Core Venues for Incubators

Business incubation can have different types of locations and can be housed in very different types of premises ranging from purpose-built new developments to converted old buildings. The location of the Oudtshoorn Tourism Incubator (OTI) as well as the Oudtshoorn Agricultural Incubator (OAI) should reflect the aims that it pursues. As with location, there is no standard type of premises to constitute an incubator. Apart from the physical size of the business incubator, a number of other physical aspects need to be considered. A key performance indicator is the occupancy rate achieved by incubation. Here a balance needs to be struck by the incubator management between maximum occupancy (and by implication rental income) and ensuring that there is sufficient flexibility to enable tenant firms to progress from one type of accommodation to another as they grow. Open-plan workspace might also be suitable since it promotes communication and interaction between tenant businesses.

Through discussions with different economic role-players, it was found that an inner-city area linked to the old train station might be suitable for small businesses in the tourism sector. As far as the agricultural incubator is concerned, the Klein Karoo
Group of companies might be of help by providing a suitable building. Their input could also be of immense value in terms of their expertise in the agricultural field.

In each of the projects, one part of the incubator should provide for manufacturing units and office space. Thus, the old railway station could give small businesses the ideal venue to manufacture their goods, using state-of-the-art equipment. They might even be able to operate on an industrial level and manufacture goods for the export market at the opportune moment in the operation of their business. The other component would be informal sales outlets as well as some curio shops. In close proximity to these outlets should be scope for more specialised tourist accommodation or transport-booking facilities and other services.

A communication system as well as transportation and sanitation facilities should form part of the physical focal areas of the incubator. The incubators for tourism and agriculture can be seen as traditional incubators that involve a number of key and potentially overlapping and flexible stages, designed to underpin the growth of clients at various stages of their development.

### 5.4 Incubation Phases and Services to be provided

The incubation process can be seen to develop through four stages, which will be briefly summarised here. They cover pre-incubation, classic incubation, graduation and the (post-incubation) phase of contact via virtual incubators.

#### 5.4.1 Pre-incubation

Pre-incubation is the term to describe support services to would-be entrepreneurs before they launch their business or join an incubator. These services include proactive identification of would-be entrepreneurs, helping them to develop a business plan, undergo basic training and getting advice on forming a company. Entrepreneurs will typically be offered desk space and other basic support such as computer and telephone access for a period. This may be up to one year in which they are expected to prepare a business plan.
The training would include monthly courses on setting up and developing new businesses and workshops on practical business topics. Entrepreneurs would also be provided with advice and assistance related to company registration procedures. These services could be provided by Red Door. Start-up entrepreneurs might therefore only enter the incubator after one to two years’ guidance from Red Door or Seda.

5.4.2 Early stage of classic incubation

The following key activities can be distinguished for this “main” phase of the incubation process.

- **Accommodation**

To accommodate tourism crafters, the incubator should consist of separate converted buildings. These should include business space for at least 20 crafters and a workshop as well as an exhibition area. The choice of premises has implications for the cost of establishing incubators. It is also important that office and workshop space ensure that units of different sizes are available to suit tenants at the different stages of growth, and that there are sufficient common facilities such as meeting rooms, cafeteria, etc. In addition, more small businesses in this sector should have the opportunity to find private, lettable space in the vicinity.

- **Networking and media exposure**

An integrated communication and networking strategy should be an intrinsic part of the initiation, development and facilitation of the business incubation strategy in Oudtshoorn. The communication function should be incorporated in the management structure of the incubation strategy. Communication will be necessary to

- mobilise local interest and co-operation,
- negotiate public-sector support,
- communicate the process and public buy-in and
- foster an entrepreneurial and innovative spirit in the area.

This will require regular networking, a dedicated page on the Oudtshoorn website and ongoing exposure in the local and district media.
A further benefit of the business incubator is the encouragement of networking between tenants themselves. It is quite common for business relationships to develop between tenants. The internal networking encouraged by the incubator is the informal cross-fertilisation of ideas and advice between tenants. The successful development of these synergies presupposes a degree of homogeneity, which in turn is a function of the business incubator’s admission criteria and its sector focus. Aside from business relationships, networking can also serve the important purpose of helping entrepreneurs to overcome a sense of isolation that is often associated with their activities. This in many respects is the greatest advantage of a physical incubator at a particular location.

- **Business support services**

  Business incubators seek to add value by offering tenants a combination of facilities and services that cannot be so easily obtained from other sources. The nature of these services and the way in which they are delivered will usually have an important influence on the success of client companies and hence on the successful performance of the incubator.

  In the case of the two proposed incubators in Oudtshoorn, the following types of services would seem to be relevant and desirable, quite aside from the provision of space through the incubator units.

  - *Ad hoc* and continuous training in basic business skills, including practical approaches to basic accounting, cash-flow management, basic legal procedures, marketing and employee relations.
  - Assistance in efforts to gain finance for business expansion, modernisation or diversification.
  - Sensitising of tenants about the availability of small-business incentives and how to apply for them.
  - Basic training and general support for prospective exporters.
  - The identification of appropriate mentors, and assistance in the financing of mentorship agreements.
  - Advice on the recruitment of staff and personnel-management issues.
Help with e-business and other aspects of ICT.
Advice on the development of new products and services.

Which of these and how much in each service category will be available in the early phase of an Oudtshoorn incubator will of course depend on the overall approach, funding and public-private sector interaction of the project. At this stage it would be precarious to forecast and promise excessively, but it would be equally short-sighted not to aim at a fairly wide range of support services to be considered and planned for.

A well-run incubator will have an operating framework setting out guidelines for its management that include a clear definition of its target market, guidelines for admission and exit rules, quality standards for client care and other aspects of the incubator’s operations as well as performance indicators against which the activities of the incubator can be monitored.

5.4.3 Graduation

Business incubation is about “hands-on support” rather than “life support”. Thus the overriding aim should be to move clients to a point where they are no longer dependent on the services of the business-incubation environment or when business incubation can no longer help them. As with selection, the exit terms and strategy should fit the business-incubation environment’s objectives, yet also take into consideration the type and profile of clients being supported. Although it is important to operate a clearly defined exit strategy, a degree of flexibility is essential as businesses will not all grow at the same rate. This raises the need for appropriate “post-incubation” services which the virtual side of the incubator has to cater for.

5.5 Virtual Incubator Thrust

As soon as core venues are finalised, one can expand these venues for businesses elsewhere to also use the services without being physically accommodated at the central incubator premises. Similarly, after businesses have reached the graduation stage they will still need assistance. These facilities and services may then still be
accessible to them. At the same time, businesses could, after exiting the incubator, plough back by offering their services to new entrants.

Some incubation environments operate with a combination of both “virtual” and “physical” provision (Business Incubation Development Framework©, UK Business Incubation Limited, 2009). In the case of Oudtshoorn, both categories of incubators suggested here should make provision for external SMME-clients. These could be small agro-processors operating outside the town or in the different suburbs. In the tourism sphere it would be B+Bs, small tour operators or crafters operating from sites away from the incubator, but being in need of specific support services only available at the centre. In fact, this concept of a virtual incubator effectively changes the relatively narrow impact of the municipal incubator (which may accommodate a mere 20 to 50 units on the premises) towards a small-enterprise-support facility for the whole town (and beyond to adjacent villages).

Naturally, there are also risks in such an opening of the target group for SMME-support services, with capacity constraints of the incubator “team” being the most important limitation. Incubator tenants will need fairly intensive, continuous support and ready access to the full range of services, which cannot be guaranteed to external enterprises hoping to be helped or proactively supported.

Financial supporters of the incubator project may be particularly sensitive about the risk of “diluting” the services available to full-time tenants due to the wider spread of support activities. Thus, the clear delimitation of support functions and target groups will be one of the critical challenges for project management.

5.6 Institutional Framework

In order to establish the business incubator in Oudtshoorn, a Section 21 company should be considered, since it has certain advantages for local economic development. It has the status of a legal person and has limited liability in the case of bankruptcy. The independence of the Section 21 company allows for flexibility and effectiveness, yet has the structure and management style of a commercial
enterprise. Disadvantages of such a model include the fact that they can be expensive and time-consuming to establish, and their structure may render decision-making quite complex. There is also the risk that due to its independence, the founders may lose control of the company. However, this should not be the case with the Oudtshoorn incubators for tourism and agriculture, if the incubator policy is outlined in detail and strictly adhered to by role-players.

Against this background a few important steps in the process of creating such an incubator can now be outlined.

5.6.1 Establishment of a policy framework

The establishment of the incubators should take place within a basic policy framework. As a first step, policy guidelines have to be established in conjunction with the initiating public-private partnerships (PPPs) and after due consideration of constraints within its organisational structure and budget.

The incubator policy framework should, *inter alia*, cover the following aspects.

- General implementation goals and principles.
- The respective roles of the Oudtshoorn Municipality, Eden District Municipality and other relevant bodies.
- Municipal regulatory controls.
- Subsidisation by the respective authorities (including Seda and/or the DTI).
- Incubation rentals and other cost-recovery principles.
- BEE policies applied to the incubator.
- Role of private sector (co-)sponsors and/or NGOs closely involved in the project.
- Sector-orientation of the core incubator.

In this context there should thus be clarity from the outset as to how the incubator process is to be structured in the Oudtshoorn area. The decision will hinge upon whether:
the Oudtshoorn Municipality wishes to establish the tourism and agricultural incubators as the focal point, with all key role-players in a supportive function, or
an autonomous incubation-centre programme is to be started with the Oudtshoorn Municipality merely playing a central supportive role in the facilitation of the specific incubator and
whether the future role of the municipality in the strategy is to be left open (and possibly changed significantly).

5.6.2 Role-players to be engaged

All relevant role-players have to be identified and their potential roles clarified. These role-players include
- the LED team of the municipality,
- council members of the municipality,
- national-government (DTI et al.) and national SMME-support agencies (like Seda),
- the Western Cape provincial government (DEDT) and provincial support agencies (like Red Door),
- the Eden District Municipality,
- SMME supportive NGOs active in the Oudtshoorn area,
- business chambers active in the Oudtshoorn area,
- Klein Karoo Group and other key corporates,
- banking institutions active in the area,
- educational institutions in the region (e.g. the South Cape FET College).

5.6.3 Information required

Serious planning for the project will require the systematic collection of data about existing SMMEs in the two target sectors for the incubator, viz. agriculture and tourism. This includes information about the range and spread of existing firms, the rate of new start-ups (and closures) in the different subsectors, key problems experienced by these firms in the area and currently assessed prospects for those subsectors. Equally important is information about the in-migration and emigration of
firms in these subsectors as well as the linkage pattern between local SMMEs and larger corporate bodies active in those sectors in the Southern Cape.

5.7 Funding of the Process

The issue of initial funding is an important one for establishing a business incubator and its future sustainability. Key partners to establish the incubators include the local and regional councils as well as representation from the private sector. There should be a strong private ethos to the incubator and its operations. The local private sector could play a role in kick-starting the entrepreneurial process in the partnership. In fact, a percentage of the set-up costs should come directly from the private sector. Getting some of the larger, local corporations on board (like KKI) could drive success, especially in the case of the agricultural incubator.

5.7.1 Capital funding

The cost for the outlay of infrastructure and financing of non-current assets are the largest capital costs. The identified municipal buildings at the train station and the inner-city premises for exhibitions might be converted according to appropriate layouts. A building for the incubator could be provided by the Klein Karoo Group. The cost to customise these buildings as well as the acquisition of the necessary equipment, needs to be financed. To the extent that incubators are viewed as a key component of local and regional economic development strategies, local and regional government should in the first instance be expected to budget for this capital expenditure.

5.7.2 Regular sources of income

The way in which business incubators are financed and the extent to which they are able to generate sufficient revenue to help cover start-up and operating costs, is a critical driver of their success. In line with the earlier overview of funding sources, the following would seem relevant for Oudtshoorn.

♦ Municipal co-funding of the annual core budget of the incubators.
Provincial- and/or national-government contributions under the different SMME-support schemes relevant for incubator clients and municipalities.

Corporate sponsorship of specific programmes or particular client enterprises.

Payment for rentals by tenants.

Cost-sharing by tenants with respect to special services.

Payroll and related staff benefits of the core staff of the incubators is likely to constitute the highest proportion of the outlay of operating costs. It is here where a longer-run commitment of core funders will be critical for the success of the project.

5.8 Managing the Project

5.8.1 Appointing a Board of Directors

It is imperative that an incubator Board of Directors be appointed at an early stage, composed of representatives of the public and private partners co-operating in the incubator. Serving on this board should be partners that provide the financial and material resources needed to establish the incubators.

The board will have to authorise the policies of the incubator, evaluate its performance and propose improvements or alterations of the incubator services. Other board responsibilities include the definition of criteria and parameters for the selection of business candidates for admission to the incubator as well as managerial supervision and the resolution of administrative questions that are beyond the purview of management.

5.8.2 Management tasks

Good planning is a crucial ingredient of incubator success. Smooth and effective administration is essential if an incubator is to be able to dedicate as much of its energy as possible in helping tenants’ businesses grow.

The appointment of a general manager would be the first step to get the process off the ground. The general manager should be in charge of setting up the incubators
and fostering their growth. The person selected will have to be able to manage the following tasks.

- Ensuring the right execution of incubator processes, through co-ordination and implementation of core activities.
- Planning, conducting, controlling and supporting the selection and recruitment of new enterprises.
- Planning, co-ordinating and following-up activities that have to support new enterprises.
- Planning, conducting and controlling the monitoring of ongoing activities.
- Establishing networks with local, regional and national as well as international SMME-support organisations.
- Administration of resources and finances.
- Supervising the programmes of incubation and entrepreneurship as well as business development.

Financial constraints will make it impossible to appoint an experienced manager for each of the two incubators, but probably only one for the whole Oudtshoorn programme. In fact, experience with South Africa’s hive programme has shown that the recruitment of adequately remunerated, competent and committed incubator managers is probably the most critical variable in the success of such programmes.

5.9 Conclusion

The quality of the management team and the support of the different role-players are critical factors in successfully establishing and operating the incubator. Business incubators are more likely to succeed if they are supported by a broadly based partnership of public and private-sector sponsors. In particular, the capacity to leverage private-sector inputs (whether this is in the form of finance or other types of support such as expertise, access to facilities or corporate subcontracting) is critical. However, it is also widely recognised that in the early developmental phase, public funding is vital, because it can often take a number of years before a business incubator can attract private-sector funding and/or generate sufficient income from other sources (e.g. rent to cover operating costs).
Given the delicate financial situation of incubator projects, it is absolutely vital that relevant public-sector levels – the local municipality, the Eden District Municipality, the PAWC and the DTI at national-government level – agree on the rationale and justification of such a project and the approach taken by the local co-ordinators. It seems equally important that the core funding (capital and annual subsidisation of running cost) does not just come from one public entity, which would greatly increase the risk of discontinued funding.

This chapter has tried to highlight key factors on the initiation of such a project. Many important aspects have only been briefly discussed or alluded to. The actual process of establishing an incubator will unfold much more dynamically in practice.
In this final chapter we want to first put the Oudtshoorn case study in a broader perspective, and then forward a range of recommendations that will, hopefully, be useful in the process of planning and implementing the Oudtshoorn incubator project.

6.1 Rationale for the Oudtshoorn Incubator

This study has started from the awareness that South Africa currently faces a number of serious economic- and social-development challenges, centring around high unemployment, unacceptably high income and wealth inequalities as well as relatively low rates of GDP growth. Together with the legacies of racial discrimination, these problems demand serious attention all over the country.

These challenges relate to the urban areas – large cities and vast township areas – as much as to the rural areas, where the emigration of skilled labour, the decline of agriculture and poor infrastructure facilities further dampen growth.

In this context, the small-business sector (i.e. small, medium-sized and micro-enterprises as well as informal-business operators) is seen to play an important role in efforts to address those fundamental problems and challenges. Creating more new enterprises, expanding existing small enterprises and strengthening their ability to face market competition and growth challenges is seen as a significant way to tackle South Africa’s employment, poverty and inequality issues.

South Africa’s small enterprises currently face many problems and challenges comparable to economies all over the world, but also shaped by South Africa’s apartheid past. Thus, to enable the small-enterprise sector to play the desired role in job creation and development stimulation, we have to address these all-pervasive problems. They relate to issues like better access to finance, information and advice, markets and business networking, to mention just the key issues.
Efforts to address these challenges come from both the public and the private sector. On the public-sector side we have the national SMME-support strategy, which includes a wide range of policies, programmes and projects, pursued through different agencies and government departments. Provincial authorities also play some role in this process, and at the municipal level SMME support constitutes an important part of all LED strategies.

On the private-sector side business associations, sector associations, large corporations (outsourcing to SMMEs), consultants and training bodies as well as the financial institutions also play important roles in the SMME-support sphere. In addition, there are NGOs which focus on SMME support, complementing the efforts of both public and private sectors.

These fairly complex processes evolve differently in the regions, cities and rural areas of South Africa. Thus, to really influence or effectively support small enterprises, we have to focus on a specific place (a city/township, town or village) in the one or other province and district of the country. In this study we have focused on Oudtshoorn as a medium-sized platteland town in the Eden District. Small-business support in this town and its surrounding areas is driven by the district and local municipalities, the dominant economic sectors (agriculture and tourism) and local business organisations, dominant firms and business leaders.

It is in this context that the incubator project, which is the focus of this study, becomes relevant and, in fact, most significant. As we can see around the world, small-business incubators have become highly rated tools or instruments to bring together clusters of small enterprises and provide them with a range of relevant and important support services.

In our study we have outlined the basic principles and operational details of incubators or “hives”, including physical centres as well as virtual incubators. We have also looked at the particular SMME scene in Oudtshoorn, and how this shapes the needs of such an incubator. This has resulted in a range of proposals for action by the relevant players if such a project is to get off the ground.
Based on this discussion in the previous chapter, the next section will summarise a set of recommendations that should help structure such an incubator initiative in Oudtshoorn.

### 6.2 Recommendations

- **Activate public debate**
  
  A small-business incubator in Oudtshoorn should be a catalyst for more active, better co-ordinated and wider-ranging SMME support in the area (Oudtshoorn and its more immediate rural surroundings). As such the idea and the possible unfolding of such a project deserves wider public debate. This should happen through the local media, municipal debates, interaction of business associations, NGOs and local business leaders as well as through discussions with district, provincial and national authorities.

  The study has shown that the financing of such a project will be a major challenge, which makes open and honest discussions between all potential funders and supporters most important.

- **Maintain a distinct sector focus**
  
  Although small enterprises are found in virtually all sectors of the economy, there is a need to give the incubator/s a distinct sector focus. This should help to mobilise public interest, attract core funding and achieve greater effectiveness.

  In our study we have concluded that agriculture and tourism should probably be the focus area for incubator initiatives in Oudtshoorn. This would, however, not exclude an incubator to accommodate a few other SMMEs, to either fill vacant space or take in promising enterprises. Besides, a dynamic incubator in one location would not preclude efforts elsewhere in Oudtshoorn to set up further clusters with different sector foci.
• **Include both urban and rural interests and needs**

Oudtshoorn is a central town in the Klein Karoo area, playing a significant role in the rural economy of the Eden District. Thus, an incubator in Oudtshoorn should not only focus on the needs and interests of entrepreneurs in the town of Oudtshoorn. It should try to also address some of the needs and concerns of the surrounding rural areas. Among others this could happen through a distinct focus on agriculture-related small enterprises (i.e. the idea of one incubator with a specific agricultural focus). On the other hand, the proposed tourism-focused incubator could also include some focus on rural or farming-based guest houses and related services, rather than only focus on activities inside Oudtshoorn or near the Cango Caves.

• **Develop the incubator as a public-private partnership**

The success of any incubator depends to a large extent on the co-operation or partnership between the key players or stakeholders. This implies first of all to the need for proactive co-operation between the public (municipality, district authorities, provincial and national departments and parastatals) and private stakeholders (like business chambers, key corporates, training bodies, consultants and NGOs).

Through such active co-operation the risk of polarisation should be overcome, i.e. the situation where specific stakeholders are either jealous of the projects (because another stakeholder seems to “own” it) or people expect, for example, “the municipality” to do all the work related to the project. If the incubator is to become a catalyst in local SMME development, such co-operation will be vital, even though will not always be easy.

• **Combine physical and virtual incubator elements**

The core of any incubator is a physical building or cluster of structures where small enterprises are accommodated (for a certain period). Such cluster may include 20 to 50 enterprises, which would be significant for a town like Oudtshoorn, but which would hardly include all the different sectors. Thus, virtual incubators have become significant, implying that SMMEs located elsewhere in or around Oudtshoorn would be able to utilise some of the support services offered
by the incubator. This could be a low-cost extension of the “reach” of the incubator, which would be particularly important for emerging enterprises in the surrounding rural areas of Oudtshoorn and the townships. In fact, in the townships such links could evolve into the creation of additional (satellite) incubators with a focus on local obstacles to SMME development.

- **Create strong leadership and management capacity around the incubator**
  Experience across South Africa (and internationally) has shown that competent leadership and effective management of an incubator is critical for the longer-run success of such a project. To attract such leadership may not be easy, given tight financial constraints, but the initiators of such a project should from the outset emphasise this condition. Here again, close partnership between public and private sectors may help to find such competent leadership [e.g. a (semi-)retired business person from one or other corporation].

- **Find the most appropriate institutional structure**
  Incubators can be closely linked to a municipality or can be owned and run on an autonomous basis, with a strong board of directors. Here again, it is important that the initiators of the project carefully consider all alternatives and decide on the most appropriate model for Oudtshoorn.

- **Mobilise funding in an incremental way**
  This last challenge (the funding of incubator-related capital and running costs) is at the same time also the greatest of the challenges. An incubator needs capital for the acquisition (and adjustment) of buildings and for common-use equipment and machinery. It needs funds for the running costs of the staff as well as core services and building maintenance as well as funds for more focused support programmes.

  In our study we have tried to show the wide range of funding sources which are available “in principle”. Whether they would be accessible for an Oudtshoorn incubator largely depends on the ability of the manager and board to mobilise these diverse funding sources – be they national, provincial, district, municipal or NGO-based. Quite logically the municipality would be expected to become a
major funder of a dynamic Oudtshoorn incubator. Yet, we have to realise that municipalities also experience tight financial conditions.

This realisation brings us back to the overall recommendation, viz. that as a catalyst in local small-business development an incubator project has to be driven by all the segments of business and civil society, which should help to tap a diversity of potentially available funds.

In essence, thus, an incubator project should be regarded as one of the most important and appropriate LED catalysts in towns like Oudtshoorn.
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