

The Allen Consulting Group

# **Evaluation of the BITS Incubator Program & the Intelligent Island Incubator**

Final Report

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Report to The Department of Communications, Information Technology and the Arts

## The Allen Consulting Group

The Allen Consulting Group Pty Ltd

ACN 007 061 930

### Melbourne

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4th Floor, 128 Exhibition St

Melbourne VIC 3000

Telephone: (61-3) 9654 3800

Facsimile: (61-3) 9654 6363

### Sydney

---

3rd Floor, Fairfax House, 19 Pitt St

Sydney NSW 2000

Telephone: (61-2) 9247 2466

Facsimile: (61-2) 9247 2455

### Canberra

---

Level 12, 15 London Circuit

Canberra ACT 2600

GPO Box 418

Canberra ACT 2601

Telephone: (61-2) 6230 0185

Facsimile: (61-2) 6230 0149

### Perth

---

Level 25, 44 St George's Terrace

Perth WA 6000

Telephone: (61-8) 9221 9911

Facsimile: (61-8) 9221 9922

### Online

---

Email: [allcon@allenconsult.com.au](mailto:allcon@allenconsult.com.au)

Website: [www.allenconsult.com.au](http://www.allenconsult.com.au)

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## Glossary

|                               |   |
|-------------------------------|---|
| Additionality                 | Outcomes achieved over and above those that would have occurred without government intervention.  |
| Angel investment              | Investment in a start-up company by an individual, usually less than \$1m.  |
| Burn rate                     | Rate at which a business (especially a start-up) spends funds.  |
| Business angel                | An individual who invests in start-up companies. Business angels are wealthy individuals who generally invest in fields they understand.  |
| Business Incubator            | See discussion of this definition in Section 2.3. Our preferred definition is: “A business incubator is an economic development tool designed to accelerate the growth and success of entrepreneurial companies through an array of business support resources and services. A business incubator’s main goal is to produce successful firms that will leave the program financially viable and freestanding.”  |
| Dealflow                      | Venture capitalists use this term to describe the flow of investment opportunities which they receive.  |
| Incubatee                     | In general usage an incubatee is a company that an incubator has agreed to provide assistance. In the specific circumstances of the BITS Incubators Program, an incubatee is a start-up company that has agreed to allocate shares to the BITS Incubator in return for incubation services and/or seed funding. The Grant Deeds define the term “Incubator Firm” as “a business that is funded by the Grantee [Incubator] with Grant monies or to which the Grantee provides services in accordance with [the] Deed”. |
| Initial Public Offering (IPO) | An offering of shares to the public for the first time – usually requiring a detailed document (prospectus) setting out details of the investment offer.  |
| Investment exit               | Incubators use this term to describe a return on capital investment. It may involve the sale of shares in a graduate or incubatee, but other forms of return are also included.   |
| Graduate                      | In general, a company which has successfully completed an incubation process (i.e. has met the agreed incubation milestones). Some BITS Incubators apply this term to individuals/companies that have successfully completed the Incubator’s business training course.  |
| Physical incubator            | A business incubator whose incubatees are physically co-located with the incubator team.  |
| Seed funding                  | The first stage of capital investment in a new company (prior to venture capital investment).   |

|                       |   |
|-----------------------|---|
| Sponsor               | Incubator sponsors usually make a contribution during incubator feasibility, start-up and/operations. Contributions may be cash, or in-kind services, personnel and equipment.  |
| Start-up              | A newly formed company.   |
| Venture capital       | Venture capital is high risk capital directed towards new or young businesses, typically between two and five years old, which are judged to have very good prospects of rapid growth and high rates of return. Venture capital involves investment not only of money but also of skills and time.            |
| Virtual incubator     | A business incubator whose incubatees are not physically co-located with the incubator team.  |
| Withdrawn (Incubatee) | In the context of the BITS Incubator Program, this category applies to companies that have withdrawn from the Incubator before completing the agreed incubation process. This may come about for reasons such as mutual agreement to cease the relationship, or because of failure to meet agreed milestones. |

## Abbreviations

|        |   |
|--------|---|
| A&B    | Allen and Buckeridge Seed Stage Ventures                          |
| ABS    | Australian Bureau of Statistics                                   |
| ACG    | The Allen Consulting Group  |
| ACT    | Australian Capital Territory                                      |
| ADI    | Australian Distributed Incubator                                  |
| ANU    | Australian National University                                    |
| ANZABI | Australian and New Zealand Association of Business Incubators     |
| ASP    | Application Service Provider                                      |
| BIF    | Biotechnology Innovation Fund                                     |
| BITS   | Building on Information Technology Strengths                      |
| COMET  | Commercialising Emerging Technologies Program                     |
| CSES   | Centre for Strategy & Evaluation Services (UK)                    |
| CSIRO  | Commonwealth Scientific and Industrial Research Organisation      |
| DAFF   | Department of Agriculture, Fisheries and Forestry                 |
| DCITA  | Department of Communications, Information Technology and the Arts |
| DITR   | Department of Industry, Tourism and Resources                     |
| FTE    | Full Time Equivalent  |
| ICT    | Information and Communications Technology                         |
| ICV    | Information City Victoria   |
| IIF    | Innovation Investment Fund  |
| IPO    | Initial Public Offering (see glossary)                            |
| IR&D   | Industry Research and Development (Board)                         |
| LAN    | Local Area Network  |
| MSD    | Management Skills Development (COMET)                             |
| NA     | Not available   |
| NBIA   | National Business Incubation Association (USA)                    |
| NSW    | New South Wales   |
| NT     | Northern Territory  |
| OECD   | Organisation for Economic Cooperation and Development             |

|      |   |
|------|---|
| OIT  | Original IT                                       |
| Qld  | Queensland  |
| R&D  | Research and Development                          |
| SA   | South Australia                                   |
| SBIP | Small Business Incubator Program                  |
| TAC  | Tailored Assistance for Commercialisation (COMET) |
| TAFE | Technical and Further Education (Institute)       |
| Tas  | Tasmania  |
| UCSD | University of California, San Diego               |
| VC   | Venture Capital                                   |
| Vic  | Victoria  |
| WA   | Western Australia                                 |

## Executive Summary

### **Introduction**

The BITS Incubator Program is part of a commitment by the Australian Government to build on Australia's information technology strengths, with funding of \$78m over four years to June 2004. The BITS Incubator Program supports business incubators that help entrepreneurs turn their technology and ideas into successful and competitive businesses.

The BITS Intelligent Island Program promotes employment growth and wealth creation in the Tasmanian economy by accelerating the growth of information and communications technology (ICT) industries. The Intelligent Island Incubator has been allocated \$8m over the same time period as the BITS Incubators. Of nearly \$85m in total funding for both Programs, almost \$70m had been paid to the Incubators at 30 June 2003.

Both the BITS and Intelligent Island Incubators provide an environment where entrepreneurial companies can obtain seed funding and develop the essential business management skills and systems that enable them to grow. The Incubators have adopted a range of models which differ significantly in some aspects, but all provide access to various types of early stage finance, make use of valuable networks, provide business coaching and mentoring and provide firms with channels to markets, including through national and international partnerships.

### **This Evaluation**

The purpose of this evaluation has been to provide advice to the Department of Communications, Information Technology and the Arts (DCITA) on the extent to which the Incubators are achieving Program objectives. The evaluation has also examined the efficiency and effectiveness of the two Programs. This evaluation follows a pilot evaluation<sup>1</sup>, also undertaken by The Allen Consulting Group, the results of which have been drawn upon in designing the present evaluation. Useful inputs, comments and advice were provided by Mr Greg Horowitz of Global CONNECT, a successful business incubator located in San Diego, as well as Mary Walshok, Vice Chancellor and Carolyn Lee, Director of Research at UCSD.

The methodology used for this study follows that of the pilot evaluation. Surveys of Incubators, Incubatees and Graduates were used to obtain data. The views of State government officials and venture capitalists were also sought.

International studies, some of which have been reviewed in this report and in the report of the pilot evaluation, have shown that business incubators are an efficient and effective way of assisting the formation and growth of new businesses. International experience suggests a number of criteria by which incubator performance can be judged.

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<sup>1</sup> The Allen Consulting Group, 2003, *BITS Incubator Program – Pilot Evaluation*, available at [http://www.dcita.gov.au/Article/0..0\\_1-2\\_11-4\\_113634.00.html](http://www.dcita.gov.au/Article/0..0_1-2_11-4_113634.00.html)

International studies show that it takes approximately eight years for business incubators to establish themselves, build a reputation and reach a point where they can demonstrate sustainability both for themselves and for their graduates. In contrast, the average period of operation of the BITS and Intelligent Island Incubators at the time of this evaluation was only three years.

The BITS and Intelligent Island Incubators have adopted a range of different business models — with the majority being for-profit and providing virtual incubation (where the Incubatees are not physically located in the premises of the incubator). The BITS and Intelligent Island Incubators were conceived in the heady days of the boom in technology shares. Initial public offerings (IPOs) of shares in new technology-based companies were a daily occurrence. The Incubators adopted business models that assumed that revenues from investment exits would be available to them from 2004. However, the subsequent sharp decline in technology share prices, accompanied by a market in which IPOs are much more difficult and less frequent, has removed this revenue source and threatens the continued viability of the Incubators.

The Incubators have encountered strong demand for assistance, with some 3,658 applications being received up to 30 June 2003. In this period, the Incubators provided assistance to 267 companies, 140 of which received assistance valued at more than \$50,000.

In addition to providing very early stage finance, the Incubators have assisted their Incubatees with business planning, financial advice, marketing, networking, mentoring, legal and accounting services, secretarial and other services — some provided from in-house resources and some outsourced.

This evaluation shows that the Incubators have been very successful in attracting in-kind support for themselves and their Incubatees from public and private sectors sources including government agencies; universities; legal, accounting and other professional service firms; business angels and venture capital firms. Up to 30 June 2003, this support was valued at \$10.5m.

During the period of this review the Incubators investments in their Incubatees included \$26.55m in cash and further \$9.83m on a charge back basis for services provided. In addition, the Incubatees received equity, loans and grants from other sources — nearly \$26m in business angel investment and nearly \$46m in venture capital investment, together with about \$12m from other sources, making total funds obtained from non-BITS sources approximately \$84m. This figure would have been higher had the R&D Start Program not been unavailable for seven months in 2002.

At the time of this evaluation the average period of incubation was only 13.5 months. In contrast, average North American and European incubation periods tend to be 3-4 years. In these circumstances the growth in employment, revenues and exports to date understate the potential of Incubatees to make significant contributions to Australia's economic growth.

While some Incubators have been more successful than others, in general, Incubator performance has been strong. Incubatees have generally rated Incubator performance well.

The evaluation concludes that the BITS and Intelligent Island Incubator Programs have performed well in the circumstances.

### ***Findings and Recommendations***

***Finding 1:*** The business models adopted by the BITS and Intelligent Island Incubators largely reflected the business conditions at the start of these Programs. The ‘tech wreck’ has had major consequences for the ability of the Incubators to raise capital and to realise some of their investments. The Incubators have had to adjust to these new circumstances and further changes may be necessary.

***Finding 2:*** There is a case for raising the present cap on investment in individual Incubatees.

***Finding 3:*** The new limited partnership venture capital funds are unlikely to have any impact before the second half of 2004 and even after that time, the extent to which they might meet the needs of the Incubators is uncertain. In the meantime the Government should provide further funding for the IIF Program and tighten the requirements for early stage investment by the IIFs.

***Finding 4:*** The BITS and Intelligent Island Incubators have adopted a variety of investment strategies. While some have concentrated their efforts on a small number of very highly prospective ICT start-ups, others have invested in companies whose prospects are more modest, but are nevertheless capable of growing to be self-sustaining, profitable businesses that create employment, and generate domestic and export revenues.

***Finding 5:*** A number of success factors have been used to evaluate the performance of the Incubators to date, including capital and in-kind contributions leveraged, Incubatee/graduate sustainability, the satisfaction of Incubatees with their incubation experience, and the extent to which Incubators have achieved self-sustaining operations. While there is some variation in performance between the Incubators, in the circumstances the overall results for the two Programs are good.

***Finding 6:*** The BITS and Intelligent Island Incubator Programs are uniquely positioned to assist start-up businesses. They provide assistance in relation to the establishment, planning, development and financing of ICT, addressing the gap between the seeds of a new ICT idea and the level at which venture capital sources will invest. There are no other government assistance programs in Australia that provide such broad-based support. The funding gap which start-up businesses face is as relevant now as it was in June 2000. The BITS and Intelligent Island Incubator Programs play a significant role in the national innovation system.

***Finding 7:*** The BITS and Intelligent Island Incubator Programs have produced hundreds of start up ICT managers who have gone through the process of starting a business and/or have gone through processes that have equipped them to grow their business to the point of achieving self-sustaining growth in revenues. While the Programs have accelerated the process of skills acquisition for some, many others owe their success to the Programs – which have also created a pool of skilled individuals with 2-3 years experience in building and operating ICT business incubators.

***Finding 8:*** Government assistance provided through the BITS and Intelligent Island Incubators has enabled Incubatees to start and develop new businesses as well as create additional ICT jobs, revenues and exports. Considering the environment in which they have operated, the Incubators have generated outcomes to date that are impressive, especially given their short period of operation and the business climate in which they have operated.

***Finding 9:*** The BITS and Intelligent Island Incubators are smaller and have operated for a much shorter period than their overseas counterparts, making comparisons problematic. A particular challenge for those Incubators not located on Australia's eastern seaboard is that they are not situated close to clusters of ICT industry activity.

***Finding 10:*** The BITS and Intelligent Island Incubators have performed well in terms of the objectives of the Programs, particularly given the short period of their operation and the prevailing business conditions. Without a further period of assistance, however, it is probable that most of the Incubators will not be viable, and a number of promising Incubatees currently receiving assistance will fail. This will result in a write off of most of the Australian Government's investment in the BITS and Intelligent Island Incubator Programs.

***Recommendation 1:*** The BITS and Intelligent Island Incubators Programs have achieved encouraging results to date and should receive further funding.

***Recommendation 2:*** The BITS and Intelligent Island Incubators Programs should be funded for at least an additional four years to give the better performing Incubators the opportunity to demonstrate success.

***Recommendation 3:*** Further funding should be based on a competitive process where Incubators demonstrate the value added they can bring to Incubatees. Basic Incubator operating costs and funds earmarked for investment in Incubatees should be separately identified. Incubatees should also be free to purchase the professional services they need either from their Incubator or from other sources. Where business training courses are available from local TAFEs or universities, they should not be provided using BITS funds.

## *Chapter 1*

# Background to the Evaluation

In June 1999, the Australian Government announced a \$158m commitment over five years to establish the Building on Information Technology Strengths (BITS) Program.

BITS aims to build the strength and competitiveness of the Australian information industries sector, including fostering much stronger commercialisation linkages with R&D organisations and the creation of clusters of innovative businesses based on information and communications technology (ICT).

The BITS initiative has three core elements:

- Incubators to assist ICT small to medium enterprises (\$78m);
- Advanced networks and Test-beds (\$40m); and
- Developing Tasmania as an 'Intelligent Island' (\$40m).

The BITS Incubator Program, funded for the four years up to 30 June 2004, has assisted the establishment of business incubators which encourage and assist the commercialisation of ideas, research and development involving information and communications technology (ICT).

The funding allows incubator managers to assist new ICT businesses at a critical stage of their development when they may be not well served by venture capital markets. The objective of the BITS Incubators is to increase the long-term success rate of new ICT-related business formation.

### **1.1 The BITS Incubator Program**

Following a discussion paper issued in September 1999, Program Guidelines were issued and applications invited.<sup>2</sup> Based on a competitive selection process, ten BITS Incubators were established covering all mainland States and Territories. In all cases, the Australian Government's BITS funding leveraged additional resources.

The ten BITS Incubators have adopted a range of models which differ significantly in some aspects, but all provide access to various types of early stage finance, make use of valuable networks, provide business coaching and mentoring and provide firms with channels to markets, including through national and international partnerships.

The Program Guidelines allow BITS Incubators to provide up to \$450,000 (and in special circumstances up to \$600,000) of BITS funding in assistance to individual start-up companies, with this assistance being through the provision of services or seed funding or a combination of both. In all cases, the BITS Incubators take an equity interest in the firms they are incubating. This equity is capped at 45 per cent with a preferred level below 35 per cent.

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<sup>2</sup> DCITA, 1999, "Building on IT Strengths (BITS) Incubator Program – Program Guidelines and Application Form", available at [http://www.dcita.gov.au/Article/0..0\\_1-2\\_1-4\\_112538.00.html](http://www.dcita.gov.au/Article/0..0_1-2_1-4_112538.00.html).

## 1.2 The Pilot Evaluation

In February 2003, The Allen Consulting Group presented the Pilot Evaluation<sup>3</sup> of the BITS Program. The objectives of the Pilot Evaluation were to:

- Provide preliminary feedback to the Department of Communications, Information Technology and the Arts (DCITA) on the progress that a sample of three BITS Incubators is making in relation to the objectives of the Program.
- Provide advice on a methodology to conduct a comprehensive evaluation of the Program in fiscal year 2003-04. That is, extrapolate the sample from three to include all 10 Incubators.
- Identify the key issues impacting on the success of the Incubators and establish whether the BITS Grant Funds are being used for the purposes prescribed in the Grant Deed.

The Pilot Evaluation examined three BITS Incubators — ITeM3 located in Sydney, Australian Distributed Incubator (ADI) in Melbourne and Playford Capital in Adelaide. It found that the Program:

- has leveraged resources from the private sector and State Government sources which appear likely to exceed Government expenditure by the end of the Program;
- has also increased the commercialisation of ICT, improved the numbers and performance of incubated businesses and increased entrepreneurship skills and specialist incubator staff able to assist start-ups;
- has led to the establishment of valuable networks with, and linkages between, global technology firms, major corporates, business advisory services, government at different levels and ICT start-ups; and
- is well managed, with Program staff demonstrating a detailed knowledge of the ten Incubators in the Program, and Incubators indicating a high level of confidence in relation to their dealings with Program staff.

## 1.3 The BITS Intelligent Island Program

The BITS Intelligent Island Program's objective is to further develop an internationally competitive ICT sector in Tasmania.

The Program has funded a range of new projects, building on the existing industry in Tasmania, Commonwealth and Tasmanian Government initiatives and the research capacity of Tasmania's education sector. The Program is overseen by the Intelligent Island Board, which is pursuing the following strategies:

- encouraging innovation and entrepreneurship;
- building the skills base;
- engaging strategic partners;
- increasing IT&T uptake in the economy generally;

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<sup>3</sup> The Allen Consulting Group, 2003, *BITS Incubator Program – Pilot Evaluation*, available at [http://www.dcita.gov.au/Article/0,,0\\_1-2\\_11-4\\_113634,00.html](http://www.dcita.gov.au/Article/0,,0_1-2_11-4_113634,00.html)

- ensuring quality telecommunications infrastructure;
- growing partnerships, networks and clusters; and
- marketing the Intelligent Island.

As part of its strategy, the Board has funded the establishment of In-tellinc, an information technology business incubator based in the Hobart suburb of Sandy Bay, that provides start-up and early stage companies with the financial resources and support necessary to realise their potential in Australian and international markets.

In-tellinc has received a commitment of \$8m for the period from June 2001 to 2005-06. The In-tellinc consortium comprises ITeM3 (a Sydney-based BITS Incubator), KPMG and the University of Tasmania. The In-tellinc Incubator shares many common features with incubators funded under the BITS Incubator Program and has therefore been included in this evaluation. When referring to the two Programs in this report we use the terminology 'BITS and Intelligent Island Incubator Programs' for convenience.

#### **1.4 Objectives of the Full Evaluation**

The objectives of this evaluation are to:

- 1. Assess progress of the ten mainland and In-tellinc incubators towards the Building on IT Strengths (BITS) Program objectives (as outlined by the Grant Deeds) which are to:
  - (a) improve the rate of commercialisation of information technology and communications ideas, research and development;
  - (b) assist eligible incubator firms (incubatees) to reach their full potential;
  - (c) play a significant role in the national innovation system; and
  - (d) have incubation centres become viable in the medium term without ongoing support from the BITS program.
- 2. Identify the key design factors impacting on the success of the incubators.
- 3. Assess the contribution of the BITS Incubator program as part of the broader range of government programs supporting start-up and early stage companies in Australia's ICT innovation system

The evaluation was asked to assess the performance of the Incubators in qualitative and quantitative terms. This included the development of performance indicators that facilitated international comparisons.

The evaluation also included an assessment of the BITS Incubator and Intelligent Island Incubator Programs themselves, including their efficiency and effectiveness.

#### **1.5 Methodology**

One of the outcomes of the Pilot Evaluation of the BITS Incubator Program was to identify the basic data that needed to be gathered from Incubators, Incubatees and Graduates for the full evaluation. Performance indicators and quality factors for the Incubators were also defined.

Subsequent to the Pilot Evaluation, the data and performance indicators were further refined in consultations between DCITA and The Allen Consulting Group. In order to collect this information, it was necessary to develop survey instruments and arrange interviews with BITS Incubator Program participants.

A review of Program documentation was also undertaken, including the agreements under which the BITS and Intelligent Island Incubators are funded, and reports provided by the Incubator managers to DCITA.

### ***Structured Questionnaires of Incubators and Incubatees***

Questionnaires were developed in consultation with DCITA and piloted on a sample of Incubators and Incubatees. Feedback from this pilot was incorporated in the questionnaire design. The questionnaire development process also benefited from feedback and advice provided by Mr Greg Horowitz, of Global CONNECT, a successful business incubator located in San Diego (see Appendix A), as well as Mary Walshok, Vice Chancellor and Carolyn Lee, Director of Research at the University of California, San Diego. The San Diego team also provided useful comments and suggestions on the draft report. Copies of the final questionnaire are at Appendix C.

The questionnaires were distributed in late July 2003 and data collected was entered into databases for analysis in August 2003.

### ***Stakeholder Interviews***

Interviews were held in August 2003 with people associated with the ten BITS Incubators and the Intelligent Island Incubator in Hobart. Those people included:

- incubator management and staff (and some Incubator Board members);
- a sample of Incubatees;
- some State government officials associated with the Incubators; and
- a number of venture capitalists and financiers associated with the Incubators.

The interviews with these stakeholders were undertaken using a semi-structured format, based on a list of questions. The interview format reflected the fact that the Incubators all took a slightly different approach to the task of helping start-up businesses to commercialise research and development and reach a stage in the development of their businesses where they can attract investment to support further growth.

The stakeholder interviews were designed to elicit qualitative information about the BITS Incubator Program that could not be readily gathered using a questionnaire alone. The interview process was also very important in providing the review team with a real world perspective on exactly how the different BITS Incubators operate.

## Chapter 2

# Business Incubators

### 2.1 Origins of Business Incubators

Business incubators have their origins in New York State, USA, when a building previously used to incubate chickens was used to provide space to start-up firms. The concept was adopted in other cities and States, but growth in the numbers of incubators was slow over the next two decades. By 1984 there were 26 business incubators in the USA. This figure grew to 550 by 1998. Today there are probably more than 3,000 business incubators worldwide.

A survey<sup>4</sup> by the USA National Business Incubation Association (NBIA) in 1998 described the key incubator statistics as follows.

- North American incubators had created 19,000 companies that were still in business and 245,000 jobs.
- The average building space occupied by an incubator was 36,657 square feet (3,405 square metres) and the median was 16,000 square feet (1,486 square metres).
- On average, incubators provided services to 20 entrepreneurial firms in 1997 (however the median was 12).

The building space statistic reflects the high proportion of traditional business incubators in the NBIA survey. The difference between the average and median numbers of firms being assisted reflects an incubator size distribution with a significant presence of larger incubators.

The business incubator concept has now spread and is widely regarded as a cost-effective approach to building new sustainable businesses with high growth potential. The justification for government support of incubators is based on systemic market failures that impact on the survival rate of new technology based firms. Because most incubated businesses remain in the region in which they started, business incubators are a favoured mechanism for encouraging local and regional development. The majority of support is provided at local or regional government level, but central governments are also involved both directly and indirectly.

### 2.2 Business Incubator Models

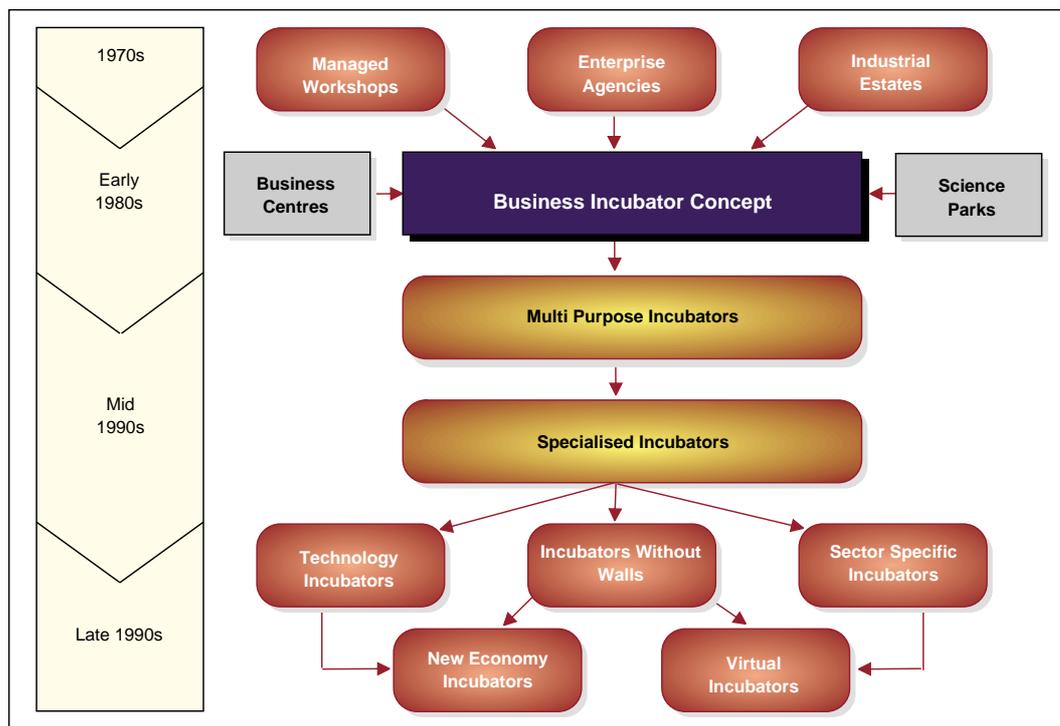
There have been a number of approaches used to classify different types of incubators. Early classifications were by origin or by lead sponsor (eg public, private, university). Other classifications have been by technology, business model (property development, venture capital), and configuration (office space, virtual).

Business incubator models have evolved over time, as illustrated in Figure 2.1.

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<sup>4</sup> National Business Incubation Association, 1998, accessed at <http://www.nbia.org/>

Figure 2.1

**EVOLUTION OF THE BUSINESS INCUBATOR MODEL**

Source: Adapted from CSES, (2002)

Since the early beginnings of business incubators, real estate has played a prominent role. Start-up companies have a limited capacity to pay rent and do not wish to enter into long-term leases. In addition, they need flexibility because their space requirements grow over time. Some business incubators have been established as part of the development of industrial parks.

The basic characteristics of business incubators have evolved over the 1980s and 1990s. The early incubators were generally public not-for-profit, fee-for-service, offering office space at a reduced cost. The growth in the numbers of virtual incubators and for-profit incubators is a recent phenomenon, and by 2000 were estimated to represent 18 per cent of approximately 3000 incubators worldwide. These two categories started to appear in the mid 1980s and their numbers expanded during the 1990s. In the 1990s, the trend was for private, business oriented, equity-for-service business acceleration. The technology business incubator emerged during the 1990s, tightly focussed on areas such as ICT and the Internet. Technology business incubators tend to be virtual and often sponsored by venture capital or multinational ICT companies.

A virtual incubator offers most of the services detailed above other than office space and on-site office services. Increasingly, business incubators charge near-market rates for their space, reducing the incentive for incubatees to take up space in the incubators. In some cities, low cost commercial accommodation is readily available, even to start-ups.

In the case of technology-based start-ups, accommodation costs are generally a small component of overall costs, and taking space in an incubator is therefore less important. In addition, when choosing accommodation, some start-ups seek locations close to their initial customers, who may be in a different location to the incubator.

Private for-profit incubators are estimated to comprise less than 8 per cent of North American incubators. These are usually established by real estate developers and, more recently, by investment groups. A year 2000 survey<sup>5</sup> by the Harvard Business School identified only 356 for-profit business incubators worldwide, of which 222 were in the USA. However, many of these have been technology business incubators and their numbers have been falling since the collapse in the market for technology stocks<sup>6</sup>.

The majority of business incubators are not-for-profit bodies sponsored by, or at least with strong links to, financial support from local and regional governments, universities and government laboratories. This is because of the perceived public benefits from business incubators. As noted previously, there is evidence that the majority of start-up firms remain in the region in which they commence operations. As a consequence, regional and local governments are often sponsors of incubators.

It might be thought that not-for-profit incubators would have difficulties in relating to their for-profit incubatees. In reality, the best not-for-profit incubators are managed on a fully commercial basis, guided by highly experienced boards and staffed by individuals with extensive private sector experience.

Another group of incubators are sponsored by businesses as a source of future business opportunities. The major sponsors are real estate developers who use the incubator as a means of attracting new companies to industrial parks. Leading technology firms comprise a second group of sponsors. These firms see incubators as a means of assisting start-ups that will develop products and services that are complementary to those of the sponsor. Venture capital groups make up the third major group of commercial sponsors. Venture capitalists see incubators as a source of investment opportunities ('deals').

In the period that the BITS Incubators were established there was a trend to for-profit, virtual incubators that were able to invest in incubatees in return for equity. These business models incorporate highly desirable features, but the sustainability of for-profit incubators is not yet proven. Incubators using this model need significant capital resources to carry them through to the point where they are receiving returns on their investments.

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<sup>5</sup> Hansen, M T, Nohria, N and Berger, J A, 2000, "The State of the Incubator Marketplace", Cambridge MA, Harvard Business School Publishing.

<sup>6</sup> Lalkaka, R, 2001, "Best Practices in Business Incubation: Lesson (yet to be) Learned", paper presented to the International Conference on Business Centres, Brussels, November 2001, available at <http://www.cses.co.uk/conferences.html>

### 2.3 Definitions

For the purposes of this report, we have used a slightly modified version of the current definition of “Business Incubator” adopted by the USA National Business Incubation Association (NBIA)<sup>7</sup>:

“A business incubator is an economic development tool designed to accelerate the growth and success of entrepreneurial companies through an array of business support resources and services. A business incubator’s main goal is to produce successful firms that will leave the program financially viable and freestanding”.

It is interesting to note the use of the term “accelerate” in this definition. Some business incubators now describe themselves as “business accelerators”.

Another definition is provided by the UK Centre for Strategy & Evaluation Services<sup>8</sup>:

“A business incubator is an organisation that accelerates and systematises the process of creating successful enterprises by providing them with a comprehensive and integrated range of support, including: incubator space, business support services, and clustering and networking opportunities.

By providing their clients with services on a ‘one-stop-shop’ basis and enabling overheads to be reduced by sharing costs, business incubators significantly improve the survival and growth prospects of new start-ups.

A successful business incubator will generate a steady flow of new business with above average job and wealth creation potential. Differences in stakeholder objectives for incubators, admission and exit criteria, the knowledge intensity of projects, and the precise configuration of facilities and services, will distinguish one type of business incubator from another”.

The term ‘graduate’ also needs to be discussed. In general usage, this term describes a company that has successfully completed incubation, usually by meeting the agreed incubation milestones. Some BITS Incubators also use this term to describe individuals or companies that have completed the Incubator’s entrepreneurship training course.

### 2.4 Services Provided by Business Incubators

As the numbers of business incubators grew from the mid 1980s, differences started to emerge in the nature of, and balance between, incubator services provided. The early incubators were based on low-cost, flexible space and shared facilities, together with some advice and other services. Today, business incubators are more diverse — so much so that there is difficulty in finding a definition that accommodates this diversity. Business incubators provide most or all of the following facilities and services, although the relative importance of these varies between incubators.

- Flexible low-cost office space with minimal lease conditions. This allows firms to acquire more space as they grow. There is usually a maximum period in which a firm can occupy space in an incubator.

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<sup>7</sup> National Business Incubation Association, 2003, available at <http://www.nbia.org/>

<sup>8</sup> Centre for Strategy and Evaluation Services (CSES), 2002, “Benchmarking of Business Incubators – Final report” for the European Commission Enterprise Directorate-General, available at [http://europa.eu.int/comm/enterprise/entrepreneurship/support\\_measures/incubators/summary\\_benchmarking\\_bi\\_2002.pdf](http://europa.eu.int/comm/enterprise/entrepreneurship/support_measures/incubators/summary_benchmarking_bi_2002.pdf)

- Office services, often on a shared basis. Commonly, these services include telephone answering; facsimile and photocopy machines; computer servers and Internet access; and the use of conference and meeting rooms.
- Business and management services. These may include: bookkeeping and accounting; a wide range of entrepreneurial training courses; advice and assistance with business planning; market analysis, investment memoranda, technical, legal and intellectual property issues; and mentoring and recruitment. Some incubators assist firms by introducing them to potential customers. In addition, incubators organise networking functions that enable incubatees to meet other firms that they can learn from and, sometimes, do business with. These functions also enable them to meet potential investors and service providers. Some incubators also organise access to workshops and prototyping facilities.
- Financial assistance and capital-raising. These services include direct financial assistance to start-ups, assistance in raising angel finance and venture capital. It involves sourcing potential investors, assisting with the documentation, presentations and the negotiation of term sheets.
- Advice on obtaining government assistance. Government assistance is an important source of financial assistance, especially for firms in technology incubators. Incubators often help firms to identify sources of government assistance and guide them through the application process.

In addition to the above, incubators commonly organise regular meetings with individual incubatees to discuss progress and monitor performance against their business plans. The extent to which Incubators should be proactive in working with incubatees is a matter of some debate. There is some anecdotal evidence that proactive incubator management may achieve better results.

## **2.5 Business Incubators in Australia**

There are 60 business incubators operating in Australia and New Zealand<sup>9</sup>. Case study material on Australian business incubators can be found in the OECD reports and in the work of Duff (1994)<sup>10</sup>. More recently, a review of business incubators in Victoria has found that many are too small to achieve self-sustaining operation<sup>11</sup>.

## **2.6 Studies of Business Incubators**

The first systemic studies on business incubators were undertaken in the mid-1980s. Until the early 1990s, most studies of business incubators focussed on incubators in the USA. Since then, there have been some significant reports from other countries including Australia<sup>12</sup>, Canada<sup>13</sup> and Europe<sup>14</sup>. Of the few international reports, two from the OECD<sup>15</sup> are relevant.

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<sup>9</sup> ANZABI, 2003, available at <http://www.anzabi.com.au/>

<sup>10</sup> Duff, A, 1994, "Best practice Incubator Management", AUSTEP Strategic Partnering Pty Ltd, available at <http://www.biaeurope.org/>

<sup>11</sup> Finney Whelan International /Allen Consulting Group/Acuity Consulting, 1998, "Building Victoria's Smart Infrastructure – A review of Victoria's Technology parks and Business Incubators", prepared for The Premier's Science, Engineering and Technology Task Force, Melbourne.

<sup>12</sup> Duff, A, 1994, *op cit*.

<sup>13</sup> Kumar, U and Kumar V, 1997, "Incubating Technology: Best practices", a report for the Canadian Federal Partners in Technology Transfer, available at <http://www.fptt-pftt.gc.ca/kumar.html>

A recent review<sup>16</sup> provides a thorough coverage of the literature. The economic benefits generated by business incubators have also been the subject of a number of articles in the literature.

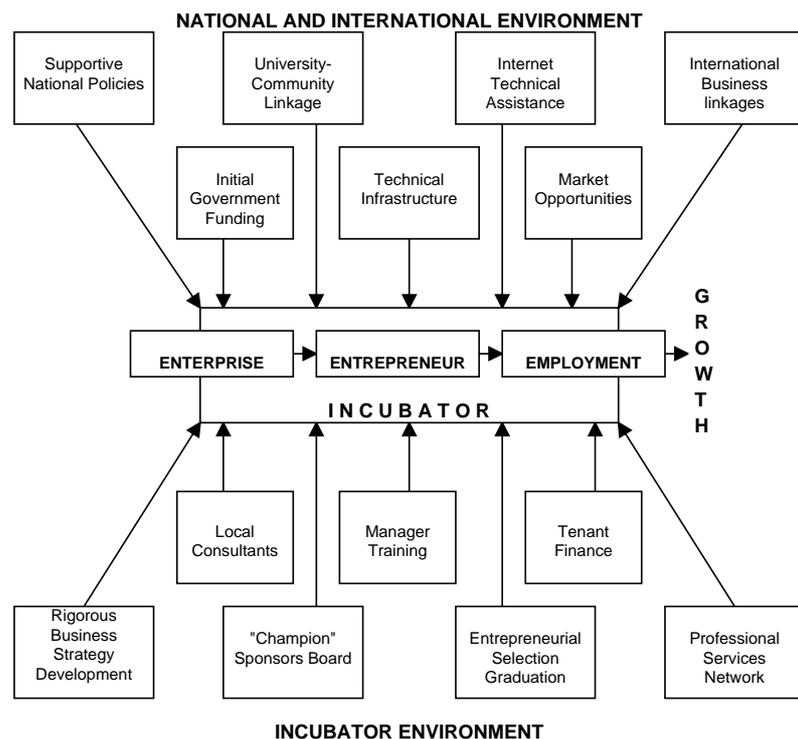
There are few studies of the financial performance of incubators. Incubator managers are often reluctant to reveal details of operational costs such as salaries paid to staff and fees paid to consultants. Income is derived from a variety of sources: various levels of government; universities; private individuals and companies (including venture capitalists); rent from the provision of office space to incubatees; fees for the provision of management and business services; royalties; and (eventually) revenue from the sale of equity in graduates. The need to maintain diversity of sources of income is discussed by Duff.

## 2.7 Features of Successful Business Incubators

One view of the features of successful business incubators is illustrated in Figure 2.2.

Figure 2.2

### INCUBATOR SUCCESS FACTORS



Source: Lalkaka, R, (1996)

A significant number of business incubators fail within their first five years of operation. Much has been written about this and the factors influencing the success of business incubators.

<sup>14</sup> CSES, 2002, *op cit*.

<sup>15</sup> OECD, 1997, "Technology Incubators – Nurturing Small Firms", and 1999, "Business Incubation – International Case Studies", OECD, Paris.

<sup>16</sup> Albert, P-A and Gaynor, L, 2001, "Incubators – Growing Up, Moving Out; A Review of the Literature", CERAM, Sophia Antipolis, France, available at <http://www.ceram.edu>

Because of Lalkaka's interest in technology business incubators, Figure 2.2 is relevant to BITS Incubators. As he has observed, technology business incubators can help overcome many of the particular problems facing technology-based start-ups, including:

- capital requirements that are higher than those of other start-ups;
- research inputs with associated technical risk;
- techno-entrepreneurs with technical expertise but lacking other necessary business skills;
- fast moving markets in which first-mover advantage can be critical to success;
- social and environmental consequences which can create additional risks; and
- the particular need for good market intelligence.

The USA NBIA addresses the qualitative factors in incubator best practice by defining two principles that characterise effective business incubation and a number of elements that contribute to these principles (Box 2.1).

Box 2.1

#### **NBIA PRINCIPLES AND BEST PRACTICE FACTORS**

##### **NBIA - Effective Business Incubation**

Principles:

- I. The incubator aspires to have a positive impact on its community's economic health by maximizing the success of emerging companies.
- II. The incubator itself is a dynamic model of a sustainable, efficient business operation.

Management and boards of incubators should strive to do the following.

- Commit to the two core principles of business incubation.
- Obtain consensus on a mission that defines its role in the community and develop a strategic plan containing quantifiable objectives to achieve the program mission.
- Structure for financial sustainability by developing and implementing a realistic business plan.
- Recruit and appropriately compensate management capable of achieving the mission of the incubator and having the ability to help companies grow.
- Build an effective board of directors committed to the incubator's mission and to maximising management's role in developing successful companies.
- Prioritize management time to place the greatest emphasis on client assistance, including proactive advising and guidance that results in company success and wealth creation.
- Develop an incubator facility, resources, methods and tools that contribute to the effective delivery of business assistance to client firms and that address the developmental needs of each company.
- Seek to integrate the incubator program and activities into the fabric of the community and its broader economic development goals and strategies.
- Develop stakeholder support, including a resource network, that helps the incubation program's client companies and supports the incubator's mission and operations.
- Maintain a management information system and collect statistics and other information necessary for ongoing program evaluation, thus improving a program's effectiveness and allowing it to evolve with the needs of the clients."

Source: NBIA, (2003)

Some selected qualitative measures that could be used in the comprehensive review of the BITS Incubator Program were also identified (Table 2.1).

Table 2.1

## Quality Factors for BITS Incubators

| Incubator Quality Issue  | Purpose of assessment  |
|--|--|
| <p><b>Governance &amp; Management</b></p> <ul style="list-style-type: none"> <li>• Appropriate legal format</li> </ul> <p><b>Balanced mix of expertise and representation on Board</b></p> <ul style="list-style-type: none"> <li>• Shared understanding of Incubator mission by Board</li> <li>• Clearly delineated roles for Board and management team</li> <li>• Management team with relevant expertise and skills capable of working effectively with incubatees</li> </ul>   | <p>Quality of management and governance is as important to Incubators as to any business.</p>  |
| <p><b>Enterprise Development Assistance</b></p> <ul style="list-style-type: none"> <li>• Performs an effective diagnostic on applicants</li> <li>• Has a full, structured array of formal/informal assistance in place to support incubatee development</li> <li>• Parallel provision of management development advice, delivered through a variety of mechanisms by seasoned business mentors</li> <li>• Has a tracking management system which monitors the effectiveness of the enterprise development assistance</li> <li>• Has a formal process that helps companies to graduate from incubation</li> </ul> | <p>The quality of assistance provided to incubatees lies at the heart of Incubator performance.</p>  |
| <p><b>Marketing Strategy</b></p> <ul style="list-style-type: none"> <li>• Knows what number of incubatees it will have when it reaches steady-state</li> <li>• Knows the type of companies it targets as prospective incubatees</li> <li>• Knows the benefits it delivers to its clients</li> <li>• Proactively manages incubatee's expectations from first contact</li> <li>• Tailors its enterprise development program to the specific needs of individual incubatee companies</li> </ul>   | <p>Incubators need to sell their services. The quality of their relations with applicants and incubatees will influence Incubator performance.</p> |
| <p><b>The Incubator facility (if applicable)</b></p> <ul style="list-style-type: none"> <li>• Has a building/facility that is attractive to its chosen market</li> <li>• Has a building/facility that provides common space</li> <li>• Has special technical facilities (eg computers, broadband access)</li> <li>• Has flexible subdivision of internal space to cater for incubatees' changing needs</li> <li>• Has a building/facility that supports the incubator's financial model</li> </ul>   | <p>The qualitative features of Incubator premises also influence incubator success.</p>  |
| <p><b>Financial Model</b></p> <ul style="list-style-type: none"> <li>• The operating budget is not burdened by expenditures arising from building/facility acquisition, refurbishment or rent</li> <li>• Incubatees experience a rent regime similar to prevailing commercial rates</li> <li>• It is free of significant internal and external risk and its revenues match or exceed expenditures</li> </ul>   | <p>Incubator financial models need to reflect international best practice.</p>   |

Source: The Allen Consulting Group, adapted from Finney Whelan et al, 1998.

Kumar and Kumar<sup>17</sup>, have reviewed Canadian incubators and assembled a list of best practices/desirable features, taking a somewhat different approach. While their approach may be of interest to incubator management it is less useful from the viewpoint of program evaluation.

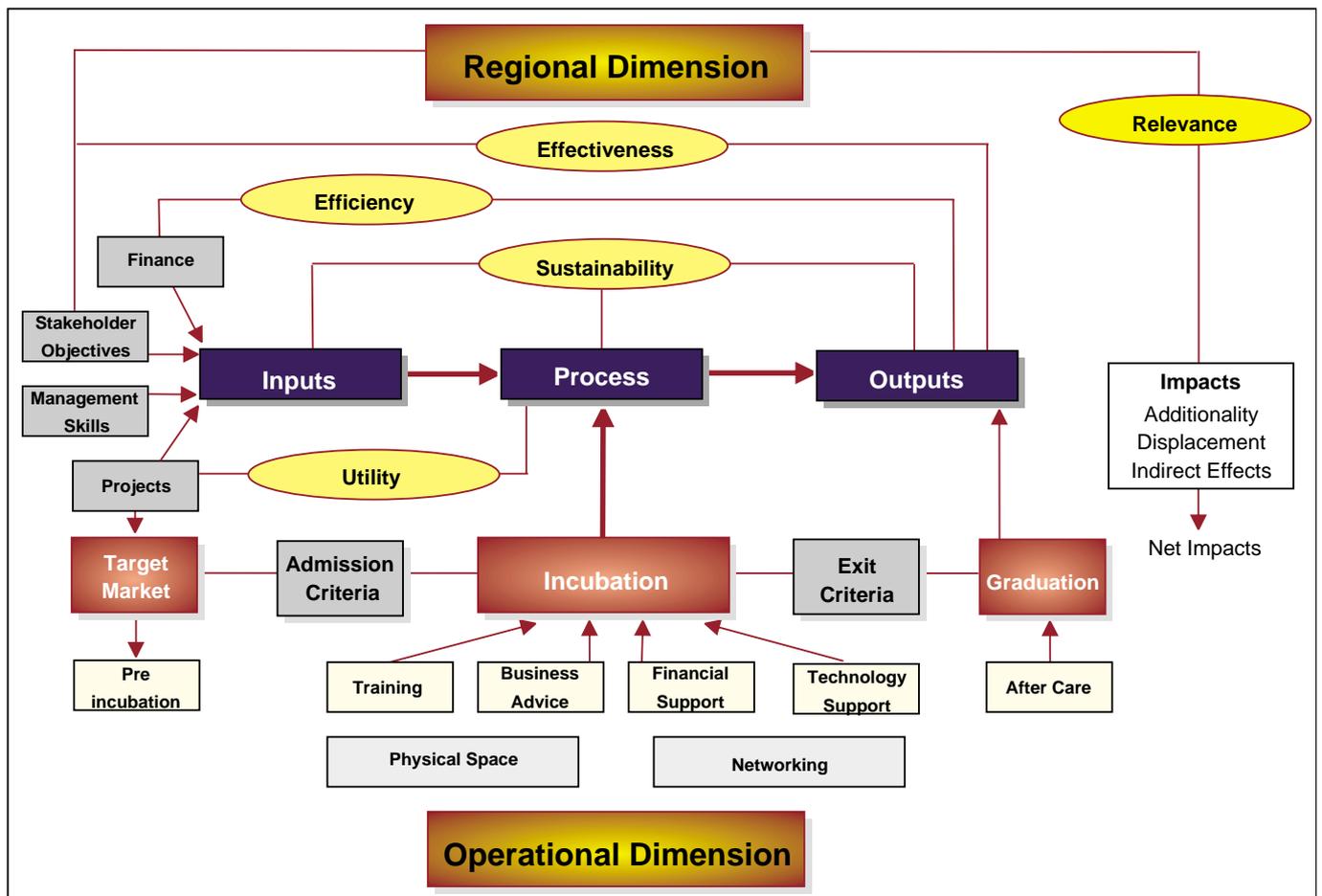
### 2.8 Benchmarking Business Incubators

Benchmarking is an important tool for assessing the performance of business incubators. Comparisons between business incubators are complicated by the wide variations in business model, country-specific variations in modality, variation in local environments and services provided. This limits the scope for comparisons but still allows benchmarking to be used to identify examples of best practice.

The most important work on benchmarking of business incubators has been carried out by the UK Centre for Strategy and Evaluation Services (CSES)<sup>18</sup> for the European Commission. CSES has developed a generic incubator model (see Figure 2.3).

Figure 2.3

#### BUSINESS INCUBATOR MODEL



Source: CSES, (2002)

<sup>17</sup> Kumar, U and Kumar, V, 1997, *op cit*.

<sup>18</sup> CSES, 2002, *op cit*.

Incubator inputs and outputs are shown in the bottom half of the Figure. The best practice issues, shown in the top half of the Figure are: efficiency, effectiveness, relevance, utility and sustainability. CSES has defined a number of key best practice issues that are used to provide a framework for defining benchmark indicators. In a BITS Incubator context, these best practice issues can be grouped under five headings.

- *Efficiency* — the relationship between financial inputs and outcomes, and value for money.
- *Effectiveness* — the extent to which the outcomes demonstrate that incubator objectives are being achieved.
- *Relevance* — the extent to which incubator objectives and outcomes promote broader government policy objectives.
- *Utility* — the extent to which services provided to incubatees meet their needs.
- *Sustainability* — the sustainability of incubator operations and the durability of outcomes being achieved (eg incubatee survival).

This leads to a definition of best practice issues in the present context (Table 2.2).

Table 2.2

Definition of Best Practice Issues

| Criteria              | Inputs and Processes  | Outcomes  |
|-----------------------|---|---|
| <i>Relevance</i>      | Incubator mission and strategy and relevance to enterprise and regional development priorities (qualitative).   | Extent to which incubator tenant characteristics match definition of target market and admission criteria (qualitative).  |
| <i>Efficiency</i>     | Financial inputs, operating procedures and unit cost of providing incubator facilities and services to client companies.  | Cost effectiveness of outputs (e.g. cost per successful business start up, cost per gross/net job created).   |
| <i>Effectiveness</i>  | Extent to which incubator achieves key operational targets set out in business plan (e.g. survival and graduation rates).   | Extent to which incubator achieves targets with regard to enterprise and wider regional development impacts (e.g. job and wealth creation).   |
| <i>Utility</i>        | Occupancy rates and take up of incubator support services.  | Extent to which incubator services meet client needs and contribute to performance.   |
| <i>Sustainability</i> | Financial sustainability of incubator (e.g. extent to which operating costs are covered by income), level of demand for incubator space and services, incubator charges compared to market rates.<br><br>Diversity of sources of incubator resources including public sector support. | Validity of incubator business strategy, diversity and continuity of income sources.<br><br>Graduation rates, retention of graduates in local area and extent to which incubators promote new start-ups in sectors of local economy with long-term job and wealth creation potential. |

Source: CSES, (2002) adapted by ACG

The CSES business incubator model highlights key performance drivers that influence the extent to which incubators achieve best practice indicators. The CSES indicators are applicable to the BITS Incubator Program and provide quantitative measures of incubator performance that can be benchmarked. These indicators represent the current state-of-the-art in performance measures. They have been used as the basis of a recent major survey of European business incubators, thus providing some useful comparisons<sup>19</sup>. The questionnaire used in that survey has some common ground with the NBIA surveys.

## **2.9 Evaluation of Business Incubators**

Evaluations of programs such as the BITS Incubator Program must largely reflect the performance of the Incubators that these programs have supported. In turn, evaluations of business incubator performance have to be judged largely by the performance of the businesses that they incubate and the extent to which they meet best practice indicators.

Benefits generated by an incubator are not usually realised in the same financial year as in which the investment is made. Thus, an evaluation can only be meaningful after a period of several years and, preferably after the incubator has reached a steady state (i.e. roughly constant rates of incoming and graduating companies).

Measuring incubator performance in terms of return on investment is complicated by the dominant presence of not-for-profit incubators. Some not-for-profit incubators are intentionally operated in a way that their costs exceed revenues from rent, services and realisation of equity. This is because many sponsors recognise the strong market failure elements in starting new businesses and are willing to underwrite running costs.

In their study, Kumar and Kumar stated that most incubator managers agree that incubators' performance evaluation criteria should include impacts on community (most commonly used criteria), financial assessment, tenants' assessment, performance versus written goals, and managers' performance.

More recently, CSES has undertaken a comprehensive survey of European incubators and their clients, covering a wider range of indicators (see Appendix D of the Pilot Evaluation Report<sup>20</sup>). These indicators provide useful benchmarks for BITS Incubators, even though some of the predominant characteristics of the BITS Incubators are different to those of a typical incubator in the European survey. In reporting the results of their survey, CSES comments on those aspects where "new economy" incubators differ from other incubators. The profile of these new economy incubators appears to closely match that of the BITS Incubators.

### ***European Survey – Incubatees and Graduates***

CSES reports a number of results that are relevant to the BITS Incubator Pilot Evaluation and are used for comparative purposes in the next Section of this report. In relation to incubatees and graduates, these results include the following.

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<sup>19</sup> CSES, 2002, *op cit*, (see Appendices to that report).

<sup>20</sup> The Allen Consulting Group, 2003, "BITS Incubator Program – Pilot Evaluation", available at [http://www.dcita.gov.au/Article/0,,0\\_1-2\\_11-4\\_113634.00.html](http://www.dcita.gov.au/Article/0,,0_1-2_11-4_113634.00.html)

- Incubatees and graduates cited the reasons for deciding to locate in a business incubator as favourable location, quality, price and flexibility of incubator space. Incubator managers generally agreed with this, but rated prestige/image ahead of the incubatee's list.
- Incubatee/graduate failure rates are also relevant, since one of the claimed benefits of incubation is a lower business failure rate. The CSES study found that 15.8 per cent of incubatees and graduates fail. This is a higher figure than that reported for the USA, but still lower than the failure rates for other businesses.
- Incubatees had an average of 7.1 employees at the time of the survey (2001). Using the average age of the incubators surveyed (8 years) and the average graduation rate (6.6 incubatees per year), CSES calculated that a typical incubator assisted the creation of 40.9 jobs per year. Using this figure, the total number of direct jobs created each year by Europe's 840 business incubators was calculated to be 34,356. Finally, this gross direct job creation was adjusted down by the failure rate to give an annual net direct job creation figure for European incubators of 28,928.
- Incubatees reported average expenditures on goods and services of €220,000 (\$A396,000)<sup>21</sup> per company in the past financial year. Taking the average annual EU wage and on-costs at €50,000 (\$A90,000), for each incubatee job, an additional 0.4 jobs were created indirectly.
- A significant percentage of incubatees reported annual growth rates of 10 per cent or more. In order to assess additionality, incubatees were asked what would have happened if they had not undergone incubation. Some 22.5 per cent of incubatees reported incubator support as critical, and a further 60.6 per cent said that it was important. The remaining 16.9 per cent believed that they would have been successful without incubation. This suggests that, for 83 per cent of incubatees, the incubation process generates net benefits<sup>22</sup>.
- The skills that incubatees value most are the ones that incubatees themselves most lack. When incubatees were asked to rate incubator services in order of importance, the results were (in declining order):
  - 1) Access to grants, seed and venture capital funding.
  - 2) Business planning and forming a company.
  - 3) Pre-incubation services.
  - 4) Training to develop business skills.
  - 5) Help with raising bank finance.
  - 6) Advice of development of new products and services.
  - 7) Other professional services.
  - 8) Advice on recruitment and personnel management.

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<sup>21</sup> The exchange rate used to convert from Euro to the Australian dollar is €1 = \$A1.80.

<sup>22</sup> This method of assessing additionality is not ideal because new incubatees tend to over-estimate benefits while graduates may do the opposite. Other published work on additionality has attempted to use control groups for comparisons. This suffers from the drawback that it is not possible to construct a control group in which the businesses provide identical goods and services to those undergoing incubation.

### **European Survey – Incubators**

The CSES survey also covered the incubators themselves and some of this information is relevant to BITS Incubators.

- Some 22 per cent of incubators, and most but not all of the new economy incubators, were reported to be for-profit.
- On average, 68 per cent of the cost of setting up a business incubator came from public subsidies and 13 per cent from private sector sponsors.
- The average incubator operating cost was reported to be €479,375 (\$862,875) per annum. Public contributions to incubators comprised, on average, 37.4 per cent of total operating costs. New economy incubators were reported to incur relatively high infrastructure and operating costs (telecommunications, computers, etc).
- Maximising revenue from rent and service charges was reported to be important for all types of incubators. Rental income and other incubator changes covered 40 per cent of operating costs and other services (including service contracts) provided a further 11 per cent.
- Some 41 per cent of incubators aimed to breakeven, expecting this to take more than five years. Most new economy incubators planned to reach a breakeven point. CSES suggests that, in hindsight, this appears to be naive given the burn rate of their incubatees. However, they point out that in the business environment prevailing in 1999, just one successful IPO could generate more than enough revenue to cover losses and failures of other incubatees.
- The average annual public operating cost subsidy per graduate job created was €4,383 (\$A7,889) (gross cost per job), which compares favourably with other forms of public intervention in Europe particularly when other factors such as indirect effects and income multipliers are taken into account. The net cost per job to the public sector was €4,065 (\$A7,317) per job. However, when contributions from all sources, as well as incubator establishment costs were taken into account, the gross cost per job rose to €4,648 (\$A26,366)<sup>23</sup>.
- The overall average failure rate of incubatees was found to be 15.8 per cent. This is lower than the failure rate for all new businesses but higher than previous studies, probably reflecting the predominance of new technology businesses and the tendency for new economy incubators to be less concerned about minimising failure. The incubators tend to take a venture capitalist view that one in ten incubatees will be successful enough to compensate for failures and still provide an adequate return on investment.

The issue of incubator financial sustainability was also reviewed in the CSES survey. Incubators were asked about the consequence of subsidies being discontinued. The responses are shown in Table 2.3. It should be noted that the result in the first line of this Table appears to be in conflict with the relative percentages of European and USA incubators reported by the CSES survey as seeking to break even.

<sup>23</sup> This is an over-estimate because no account was taken of taxes paid by incubator employees.

Table 2.3

## Effect on Incubator Operations if Cash Subsidies Ceased

| <b>Financial Sustainability</b>                                    | <b>Europe (%)</b> | <b>USA (%)</b> |
|--|-------------------|----------------|
| <i>Incubator activities could be maintained at current level</i>   | 7.7               | 17.3           |
| <i>Incubator activities would have to be significantly reduced</i> | 39.7              | 23.1           |
| <i>Incubator activities would stop altogether</i>                  | 21.8              | 13.5           |
| <i>Not relevant – incubator does not receive subsidies</i>         | 11.5              | 34.6           |
| <i>No response</i>   | 19.2              | 11.5           |
| <b>Total</b>   | 100.0             | 100.0          |

Source: CSES, (2002)

As Table 2.3 shows, 76 per cent of European respondents and 41 per cent of USA respondents indicated that their Incubators needed continuing subsidies. A 1997 NBIA study<sup>24</sup> reported that 78.4 per cent of sponsors provided an annual operating subsidy for business incubators. Sponsors included city, county and state governments (29.7 per cent); universities (27 per cent); multi-entity consortia (18.8 per cent) and economic development organisations (16.2 per cent).

<sup>24</sup> Molnar, L A, Grimes, J E, Edelstein, R De P, Sherman, H, Adkins, D and Tornatzky, L, 1997, "Business Incubation Works", NBIA Publications.

## *Chapter 3*

# The BITS and Intelligent Island Incubators

### **3.1 Introduction**

This Chapter presents facts and figures about each of the Incubators examined in the evaluation. It reflects information provided by the Incubators in their responses to the Incubator questionnaire, comments by Incubatee questionnaire respondents and interviews with the management of the Incubators.

The information is presented in somewhat of a standardised format for ease of reading, although caution should be taken in comparing the performance of each of the Incubators across the performance indicators. For instance, while information was sought about the change in total Incubatee employees (from the start of the Program until 30 June 2003), in some cases it was necessary for the Incubators to advise their Incubatees to either reduce full time employment or bring in contractors as a way of putting their businesses on a more sustainable footing. In this regard, an unspectacular increase in employment does not necessarily mean poor performance.

In this Chapter, the term ‘charge back basis’ is used to describe the arrangement used by some of the Incubators, where services to the Incubatee are charged against credits held by the Incubator on the Incubatee’s behalf.

### **3.2 Allen & Buckeridge Seed Stage Ventures — NSW**

#### ***Introduction***

Allen & Buckeridge Seed Stage Ventures (A&B) is a virtual Incubator based in the Sydney central business district. It is embedded in the venture capital investment activities of the Allen & Buckeridge Group, which manages some \$A250 million of equity funds focused on seed and early stage ICT industry companies in Australia. A&B’s intent was to balance current year revenues and expenses so that profit would solely come from capital gain on equity in successful businesses. A&B claims that it will be subsidising its last year of (BITS) operations.

While it began operations with seven FTE staff, A&B now is serviced part-time by the seven venture capital professionals in the group — effectively only one FTE person. Its investment model is a blend, where 6 Incubatees have been provided with a mix of equity cash (75 per cent) and services (25 per cent) and 20 other projects have been provided services only, which have been expensed by the Incubator. Over 26 projects equity cash has been 42 per cent of direct funding.

Its Incubatees are able to choose A&B’s own professional service providers, or to select from any of the professional service firms with which A&B has special arrangements.

Incubatees that receive less than \$50,000 in investment stay with A&B for an average of 3 months, whereas those that receive more than \$50,000 in investment stay for an average of 6 months. Many of A&B's projects did not use agreements as a graduation trigger. The performance indicators used by A&B include being successful in self-funded growth or achieving growth through capital raised from other sources other than BITS.

A&B sources most of its Incubatees through ICT industry contacts or networks (80 per cent) or from Universities, government labs and CRCs. This is assisted by its related venture capital activities.

DCITA's view is that A&B has accepted 13 companies, graduated five companies and had seven companies that withdrew from incubation up to 30 June 2003.<sup>25</sup> A&B takes a different view and reports higher figures. DCITA and A&B are currently discussing this matter. In this report the figures used have been provided by DCITA.

### ***Financial Information***

A&B received \$4.9m of its \$5m BITS allocation up to 30 June 2003. Some 31 per cent of the \$4.7m of funds expended to 30 June 2003 was provided to Incubatees as cash investment.

A&B estimates that it has leveraged:

- in-kind contributions valued at around \$25,000;
- other financial contributions of around \$1.1m; and
- additional equity investment (received by its Incubatees) of \$25.7m that it had a facilitating role in, most of which came from third party venture capital funds and corporate investors.

A&B estimates that it incurred \$150,000 in costs in its initial application for BITS funding and \$100,000 in costs in meeting reporting and other DCITA requirements.

Set up costs were estimated at around \$700,000 with the major impost being in respect of initial staff recruitment costs (90 per cent). Running costs averaged around \$1.15m per year over the last three years, with average payroll costs accounting for 45 per cent of BITS funding received.

The average rate of equity it takes in its Incubatees is five per cent, most having issued no equity, but it has taken up to 30 per cent in the six companies that have issued shares to the Incubator's investment vehicle, ePark Direct Equity Fund Limited.

To 30 June 2003, A&B has had no investment exits and no trade sales. It reports that six of its Incubatees are trading as corporations, four are growing in 2003-04, and that all six in aggregate are generating 60 per cent of their revenues from overseas in 2002-03.

A&B reports that these six Incubatees have achieved the following outcomes to 30 June 2003:

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<sup>25</sup> A&B takes the view that the considerable due diligence work undertaken in respect of many prospective investments constituted incubation.

- Employment has risen from 28 to 69 FTE.
- Total revenue has risen from zero to \$2,910,000.
- Total export revenue has risen from zero to \$1,750,000.

### ***Quality Factors***

A&B has a separate Board (with two independent directors) that meets quarterly.

It has links with external professional service providers and is able to get deals for its Incubatees at less than market rates. It also has a network of external professional capital providers (angel investors) that specialise in the financing of start up companies.

A&B's financial model is not significantly burdened by expenditures arising from building/facility acquisition, refurbishment or rent. As a virtual Incubator, A&B is not subject to large internal risk because it does not rely on tenants for its revenues.

Prospective Incubatees are given assistance with the development of a business plan and the development of their business proposals. Business training programs are occasionally conducted in-house and outsourced.

A&B's management team appears to have relevant expertise and skills capable of working effectively with Incubatees. It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers an outsourced, formal business development training program to its Incubatees, and informal business training is provided in-house.

Other in-house services provided by A&B to its Incubatees include:

- advice with business planning;
- financial management advice;
- marketing and sales services;
- networking opportunities; and
- use of meeting rooms.

As a virtual Incubator, A&B does not provide physical space to its Incubatees.

A&B manages a BITS dedicated investment fund — its own ePark Direct Equity Fund, which has been capitalised at \$1.4 million, being the after-tax retained capital following receipt of \$1.9 million of the BITS grant.

### ***Comments by Incubatees***

Some 67 per cent of A&B's Incubatees that received significant assistance and five per cent that received limited assistance responded to the questionnaire. Most respondents rated A&B's performance in respect of the services they received as being (on average) either good or very good.

A&B did not provide in-kind services to its Incubatees on a charge back basis, so the survey question relating to value of these services was not relevant.

Most of the comments received from A&B Incubatees were positive. The following statements by A&B Incubatees are typical of the comments received.

A&B have very good business experience and principals and were energetic and responsive to our needs

Without them we could not of commercialised our technology. They add credibility and substance to a start-up

A&B Incubatees

### ***A&B's Perspective***

A&B management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

A&B expects that its activities for BITS-eligible private sector funds will need to be reduced significantly and that it would require further funding for equity investment activities once BITS funding ceases on 30 June 2004. Public sector projects requiring seed finance and incubation assistance are now being serviced by a pre-seed fund that is managed by the A&B full-time venture capital professional team

A&B's BITS program was the smallest grant awarded and more than \$600,000 has been paid back to the Government in taxes. A&B believes that it was never of a scale to be a stand-alone activity and only made sense as a precursor to funding by A&B managed venture capital funds, hence the small number of Incubatees (6) that have received equity investment from the ePark Direct Equity Fund.

### ***Overall Assessment***

A&B have sought to focus their incubation activities on Incubatees that have the potential to grow their annual turnover to around the \$100m mark. As a consequence, they have accepted fewer applicants for incubation and this, coupled with A&B's strong reputation as an ICT specialist venture capital investor has enabled their Incubatees to raise significant amounts of capital.

## **3.3 Australian Distributed Incubator — Victoria**

### ***Introduction***

The analysis in this report applies to the operations of Australian Distributed Incubator (ADI) up to 30 June 2003. On 27 June 2003, ADI was acquired by Business Strategies International<sup>26</sup> (BSI) and the former manager of ADI's Sydney operations took over as CEO. The entire ADI portfolio was sold to Jolimont Ventures<sup>27</sup>, a consortium led by ADI's founding CEO and Investment manager. Jolimont will continue to provide services to this portfolio and will provide reports to DCITA.

ADI is a for-profit, virtual Incubator based near the Melbourne CBD and operating across Australia. Since it opened its doors, ADI has reduced full time staff from four to one FTE. Its investment model has involved a blend, where Incubatees are provided with a mix of assistance (generally 75 per cent cash and 25 per cent services).

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<sup>26</sup> BSI is a multidisciplinary company focusing on high growth SMEs, which are assisted through mentoring, raising capital, grants and tax incentives and business advice.

<sup>27</sup> Jolimont Ventures is backed by Quay Partners, Starfish Ventures and Babcock & Brown. Starfish manages the JAFCO Investment (Asia Pacific) Australian fund. Starfish also operates a \$24m Pre-Seed Fund.

Its Incubatees are able to choose ADI's own professional service providers, or to select from any of the professional service firms with which ADI has special arrangements.

Up to 27 June 2003, Incubatees that received limited assistance stayed with ADI for an average of 6 months, whereas those that received more than \$50,000 in assistance stay with ADI for an average of 12 months. Graduation was achieved at the end of the Incubator agreement and at the completion of a structured business development training program. ADI sourced most of its Incubatees through ICT industry contacts or networks.

ADI has accepted 88 companies (14 received more than \$50,000 and 74 received less than \$50,000 of investment) and graduated 50 companies (10 that had received more than \$50,000 and 40 that had received less than \$50,000) up to 30 June 2003. Of the 14 companies that received significant assistance from ADI, 12 were still trading at 30 June 2003.

### ***Financial Information***

ADI received all of its \$7m BITS allocation up to 30 June 2003. At that date some 34 per cent of the \$5m of funds expended had been provided to Incubatees as cash investment. ADI estimates that it has leveraged:

- in-kind contributions valued at \$3.2m, all of which were provided to the Incubator;
- other financial contributions of \$705,000, mostly Victorian Government funding; and
- additional investment (received by its Incubatees) of \$9.9m that it facilitated. ADI co-invested with InQbator in Genetraks, which successfully raised \$7.6m in venture capital.

ADI estimates that it incurred \$30,000 in costs in its initial application for BITS funding and \$180,000 in costs in meeting reporting and other DCITA requirements.

Set up costs were estimated at \$100,000 with the major impost being in respect of other setting up costs (47 per cent) and preparation of legal documents (29 per cent). Running costs averaged around \$1m per year over the last three years, with average payroll costs accounting for 22 per cent of BITS funds received. Through synergies with BSI, ADI's future running costs are expected to be significantly lower.

The average rate of equity ADI takes in its Incubatees is 15 per cent, although it has taken equity rates as low as 2 per cent and as high as 31.4 per cent. Up to 27 June 2003, ADI has had no investment exits and no trade sales.

ADI reports that its Incubatees have achieved the following outcomes to 30 June 2003:

- Employment has risen from 100 to 125 FTE.
- Total revenue has risen from \$4m to \$5m.
- Total export revenue has risen from \$100,000 to \$125,000.

### **Quality Factors**

During the period there were six people on the ADI Board including an independent Chair. The Board met monthly for the first two years of ADI's operation, and since that time has met around six times per year. The Board has an investment committee that meets separately from the Board meetings. There seems to be a clear separation between the Board and management.

ADI has a network of external professional service providers that includes accountants and legal advisors. Its Incubatees can access these and receive a 25 per cent discount on fees.

Prospective Incubatees are given assistance with the development of a business plan. Many of ADI's business readiness services were outsourced to various providers. Since the BSI takeover, these services and quarterly Investor Forums are provided by BSI's business advisory group.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers an outsourced, formal business development training program to its Incubatees.

Other in-house services provided by ADI to its Incubatees include:

- advice with business planning;
- financial management advice;
- marketing and sales services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

As a virtual Incubator, ADI did not provide physical space to its Incubatees. Since the takeover by BSI, two new portfolio companies are housed on the premises of the Incubator. ADI has helped secure office space through relationships with real estate agents and various programs such as the City of Melbourne's small business office establishment grants.

In the review period, ADI did not develop a close relationship with an investment fund, but sought investment capital from various sources on a case-by-case basis. Since the change of management, relationships have been established with a number of investment funds.

### **Comments by Incubatees**

Some 57 per cent of ADI's Incubatees that received significant assistance and three per cent that received limited assistance responded to the questionnaire. Most respondents rated ADI's performance in respect of the services they received as being (on average) either good or very good.

A majority of Incubatee respondents to the questionnaire commented that they thought that the in-kind services provided by ADI on a charge back basis represented value for money.

Most of the comments received from ADI Incubatees were positive. Most commented on the high quality of the advice received, but noted the restrictions associated with the funding limitations. The following statements by ADI Incubatees are typical of the comments received.

Raised awareness of what is required and taught me skills to differentiate between excellence and snake oil in future service providers.

The advice and mentoring we have received from ADI has been invaluable. We now have a clear path to market for our .... product. In addition, we've been introduced to senior executives of potential partners such as Telstra and Sony that we would have had difficulty getting to on our own.

ADI Incubatees

### ***ADI's Perspective***

ADI's previous management are of the view that its original business plan was sound in providing the right mix of cash and services and ensuring that grant money was efficiently spent. ADI's current management have repositioned ADI as a low cost incubator where the bulk of the capital is directed towards investment.

However both the previous and current management note that two factors were delaying the outcomes they had expected in terms of business growth and exits. These were the downturn in the ICT industry and the difficulty, in general, of attracting additional venture capital although, in this respect ADI has been particularly successful in achieving co-investment of \$9.9m alongside its own direct investment of \$1.8m. ADI's current management believe that the investment climate is changing and that ADI is well placed to fulfil the original vision behind the creation of the BITS Incubator Program.

ADI believes that its operation's strengths include:

- an ability to attract capital for its Incubatees from external sources;
- a trusted, hands-on management team;
- an ability to rapidly start operations for new companies – little infrastructure is needed; and
- pragmatic, creative deal-making; broad networks; high throughput per FTE, maximising the number of companies to benefit from government funding.

ADI reports that the weaknesses of its operation were a lack of available co-investment and a lack of funding available for follow-on investment. This will now be addressed through the ADI-BSI Investment Forum.

### ***Overall Assessment***

For the period under examination, ADI performed reasonably well in terms of assisting its Incubatees to raise capital and build their businesses. It is not clear how successful those ADI Incubatees that received limited assistance have been because they have proved difficult to track down, despite efforts to find them.

### **3.4 BlueFire — New South Wales**

#### ***Introduction***

BlueFire is a for-profit, mixed Incubator (physical and virtual) based in Sydney. Over the period that it has operated, BlueFire has reduced its full time staff from six to two FTE. Its investment model is cash only where seed funding is provided to Incubatees who in some cases may buy back services from the Incubator. That is, its Incubatees are able to buy professional services from BlueFire, or select from the professional service firms with which BlueFire has special arrangements, or choose other service providers. The Incubatee respondents to the questionnaire said that they thought that the services provided by BlueFire represented value for money.

While BlueFire has not charged for services provided to its Incubatees, it has flagged the possibility of charging its Incubatees for services post 30 June 2004 on a retainer or project basis. It claims to have had a positive response to this proposal from its existing Incubatees. It prefers this kind of arrangement because it puts all dealings between the Incubator and Incubatees on a commercial basis.

Incubatees that receive less than \$50,000 in investment stay with BlueFire for an average of 6 to 12 months, whereas those that receive investment of more than \$50,000 stay for an average of 12 to 18 months. Graduation is achieved when Incubatees generate significant revenue, small profits are made, or when a significant scaling back of BlueFire's involvement is achieved.

Graduation is achieved at the end of the Incubator agreement. BlueFire sources most of its Incubatees through industry contacts or networks.

BlueFire has accepted 13 companies (2 that received less than \$50,000 and 11 that received more than \$50,000) and graduated three companies (all of which had received more than \$50,000) up to 30 June 2003. All three of its graduates are still trading. Three companies have withdrawn from incubation.

#### ***Financial Information***

BlueFire received nearly \$4.3m of its \$6m BITS allocation up to 30 June 2003, 60 per cent of which was provided to Incubatees as cash investment. BlueFire estimates that it has leveraged:

- in-kind contributions valued at \$600,000, 50 per cent of which have been provided to its Incubatees;
- other financial contributions of \$563,000, most of which was received from shareholders/guarantors; and
- additional investment (received by its Incubatees) of \$3.7m that it had a facilitating role in, most of which came from business angels.

BlueFire estimates that it incurred \$100,000 in costs in its initial application for BITS funding and \$200,000 in costs in meeting reporting and other DCITA requirements.

Set up costs were estimated at \$650,000 with the major impost being in respect of other setting up costs (75 per cent). Running costs averaged around \$434,000 per year over the last three years, with average payroll costs accounting for 18 per cent of the BITS grant received.

The average rate of equity BlueFire takes in its Incubatees is 10 to 15 per cent, although it has taken equity rates as low as 8 per cent and as high as 25 per cent. To 30 June 2003, BlueFire has had one investment exit, which was a scrip-for-scrip trade sale in the USA.

BlueFire reports that its Incubatees have achieved the following outcomes to 30 June 2003:

- Employment has risen from 5 to 52 FTE.
- Total revenue has risen from zero to \$9.8m.
- Total export revenue has risen from zero to \$1.67m.

### ***Quality Factors***

The management of BlueFire and its Board are separated with the Board comprising a majority of non executives, although the Chief Executive Officer also sits on the Board. It also has a broadly based external advisory arm that acts like an investment committee. The external advisory arm meets with management three to four times a year. The Board operates under a code of corporate governance/ethics.

BlueFire's management team appears to have relevant expertise and skills capable of working effectively with Incubatees.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers occasional business training sessions to its Incubatees, with some outsourced and other provided in-house.

Other in-house services provided by BlueFire to its Incubatees include:

- advice with business planning;
- financial management advice;
- marketing and sales services;
- secretarial services;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

It has 100 square metres of space available for resident Incubatees, which equates to around 20-70 square metres per Incubatee plus a common space. BlueFire facilities include office services and equipment, server and LAN facilities plus high speed Internet access.

While BlueFire has not developed a close relationship with an investment fund, it claims to have developed relationships with a number of venture capital providers. It still shops around on a case-by-case basis for the best investment deals it can find. BlueFire believes that aligning itself with one fund makes it very difficult to raise money if that fund chooses not to invest and that venture capital investment decisions are based 95 per cent on the merits of the opportunity itself and very little on the source of the dealflow.

### ***Comments by Incubatees***

Some 64 per cent of BlueFire's Incubatees that received significant assistance and none that received limited assistance responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) either good or very good. BlueFire did not provide in-kind services to its Incubatees on a charge back basis, so the survey question relating to value of these services was not relevant.

A majority of the comments received from BlueFire Incubatees were positive. The following comments by a BlueFire Incubatees are good examples of how the BITS Incubator Program has had a positive impact, particularly in respect of encouraging and assisting activity that might otherwise have not occurred.

Incubation funding has specifically allowed us to lodge IP patents and pursue sales and marketing opportunities that otherwise would have been foregone. Appropriate and timely funding has been a real strength of our incubation experience. No weaknesses have been identified.

Have learnt a lot about running a business properly. Company has received excellent marketing collateral.

BlueFire Incubatees

### ***BlueFire's Perspective***

BlueFire management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

It believes that its strengths lie in it having lean structures, genuine entrepreneurial experience in IT start ups, and its ability to provide sound, independent analysis. It notes the challenge involved in finding opportunities that satisfy its criteria over the grant period.

BlueFire has been able to engage the local business community through legal services from Blake, Dawson, Waldron, IT equipment from Sun Microsystems and time and advice from mentors.

If BITS funding ceased post 30 June 2004, BlueFire expects that its activities would need to be reduced significantly, and that it would require further funding and would take at least 12 months to be viable.

### ***Overall Assessment***

The BlueFire Incubator has performed reasonably well over the period examined. In the Sydney market where there is some investment capital, it was not as successful as it would have wished in raising significant amounts for its Incubatees. It received favourable comments from its Incubatees, which welcomed BlueFire's approach.

### **3.5 EiR — Western Australia**

#### ***Introduction***

EiR is a for-profit, mixed Incubator (physical and virtual) based in Perth. Since it began trading, EiR has slowly built up its full time staff from one to three and a half FTE. Its investment model is a blend, where Incubatees are provided with a mix of cash and services, with the services provided on a charge back basis.

Its Incubatees are able to choose their own professional service providers, or to select from a number of professional service firms with which EiR has special arrangements.

Incubatees that receive less than \$50,000 in investment stay with EiR for an average of 6 months, whereas those that receive more than \$50,000 in investment stay with EiR for an average of 18 months. Graduation occurs at the achievement of agreed milestones in the investment subscription agreement.

EiR sources most of its Incubatees through industry contacts or networks. EiR has accepted 17 companies and graduated six companies up to 30 June 2003. The six graduates are still trading.

#### ***Financial Information***

EiR received \$7.5m of its \$10m BITS allocation up to 30 June 2003. Some 49 per cent of the \$6.3m of funds expended to 30 June 2003 was provided to Incubatees as cash investment. EiR estimates that it has also leveraged:

- in-kind contributions valued at around \$475,000, 70 per cent of which have been provided to its Incubatees;
- other financial contributions of \$802,810 (largely made up from a Western Australian Government grant and building management and Internet services income); and
- additional investment (received by its Incubatees) of \$5m that EiR had a facilitating role in. Most of this investment came from business angels, venture capitalists and other government sources.

EiR estimates that it incurred \$130,000 in costs in its initial application for BITS funding and \$278,000 in costs to date in meeting reporting and other DCITA requirements.

Set up costs were estimated at \$70,000 with the major impost being in respect of initial staff recruitment costs (29 per cent) and preparation of legal documents (26 per cent). Running costs averaged just over \$1m per year over the last three years, with average payroll costs accounting for 24 per cent of the BITS funds received and tax paid has been 21 per cent of BITS funds received.

The average rate of equity it takes in its Incubatees is 20 per cent, although it has taken equity rates in its Incubatees as low as 6.5 per cent and as high as 45 per cent. To 30 June 2003, EiR has made three partial investment exits, realising \$242,000.

EiR reports that its Incubatees have achieved the following outcomes to 30 June 2003.

- Employment has risen from zero to 50 FTE.

- Total revenue has risen from zero to \$1.8m.
- Export revenue has risen from zero to \$100,000.

### ***Quality Factors***

EiR appears to have a fairly broadly based Board, with experience ranging from small businesses, technology park management, to software engineering and finance. The Board has a separate investment committee. Board members have a role in Incubatees, effectively acting as project directors.

EiR also has links with external professional service providers such as accountants and legal advisers. EiR's management team appears to have relevant expertise and skills capable of working effectively with Incubatees. Around 80 per cent of management time is spent with Incubatees, with around 20 per cent spent on administration.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. In respect of a business development training program, it offers occasional sessions conducted in-house.

Other services provided in-house by EiR to its Incubatees include:

- advice with business planning;
- financial management advice;
- legal or accounting services;
- a mentoring program;
- marketing and sales services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

EiR has 600 square metres of space available for resident Incubatees, which equates to around 100 square metres per Incubatee plus a common space. EiR's facilities include office equipment, server and LAN facilities plus high speed Internet access.

EiR has not developed a close relationship with any specific investment fund, preferring to shop around on a case-by-case basis for the best investment deals it can find.

EiR is not subject to major external risk in respect of its accommodation arrangements because of an accommodation subsidy paid by the Western Australian Government. It has no 'anchor tenant' that it relies on in relation to revenues.

### ***Comments by Incubatees***

Some 60 per cent of EiR's Incubatees that received significant assistance and 71 per cent that received limited assistance responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) good.

EiR did not provide in-kind services to its Incubatees on a charge back basis, so the survey question relating to value of these services was not relevant.

Most respondents noted the strong support received and the credibility that EiR brought to their projects. None of the respondents could suggest a required service that was not already being provided by EiR. Most were in agreement that the main weakness of their incubation experience was that the amount of capital provided was insufficient.

The majority of the comments received from EiR Incubatees were positive. The following statements by EiR Incubatees are typical of the comments received.

Strengths: people and the experience and advice they provided. Weaknesses: funding limitations of the BITS Program and limited resources (people and funds) within EiR.

EiR provided support during difficult periods in commercialisation, for example, periods of low cash flow.

EiR Incubatees

### ***EiR Perspective***

After an initial period of instability at the beginning of the grant period that involved significant changes to management, EiR believes that it now has in place a viable business operation. EiR advises that it has positioned itself financially to be able to operate beyond the expiration of the BITS grant period, although it regards itself as still a few years away from the possibility of self sustainability.

EiR lists the strengths of its operation as being able to use the BITS funds effectively to leverage state and private funds. It also claims to have strong networks in regional and international arenas — including markets, technology transfers and private equity. It believes that it is a unique provider in the small WA market and that it has an experienced team in structuring and mentoring and commercialisation programs for start up companies. It also provides sound commercial and business acumen to (in the most part) technical Incubatees.

EiR lists its weaknesses as being unable to fully fill the gap between its ability to capitalise Incubatees and the level that is required to interest venture capitalists. It also claims that it has insufficient BITS funds to service its deal flow.

It believes that there are a number of characteristics of the region that it is physically located in that present challenges, including:

- no other Seed Funds in the region;
- a lack of investment funds to service demand in region;
- a relatively small market;
- a small number of corporate players in market;
- traditional markets are agriculture and resources;
- a high level of interest being taken to diversify traditional markets;
- WA being a largely SME marketplace;
- the culture of WA business being to act globally as a necessity;
- Perth being a gateway to South East Asia and Europe;

- a relatively low cost base for company operations; and
- distances from traditional ‘major’ markets in Australia being sometimes a barrier to growing businesses.

EiR has been able to gain support from the local business community through encouraging some of them to participate as Board members for Incubatee companies. It has received support with introductions and networks for Incubatees and with the raising of other private funds.

EiR expects that it could maintain its activities at or near current levels beyond 30 June 2004. EiR will continue to invest in new start-ups but at a reduced investment level until EiR realises current investments. However, it can imagine insufficient seed level funds to service deal flow without further BITS funding.

### ***Overall Assessment***

EiR has experienced challenges in raising capital for its Incubatees, reflecting the difficulty of finding co-investors interested in ICT in Western Australia. It has performed well considering that it is situated so far away from the larger ICT markets of the eastern seaboard. Its performance has also been good considering the changes to the Incubator team and Board that have occurred.

## **3.6 Epicorp Limited — Australian Capital Territory**

### ***Introduction***

Epicorp is a not-for-profit, mixed Incubator (physical and virtual) located on the CSIRO’s Black Mountain site, across the street from the ANU campus in Canberra. Since it opened its doors, Epicorp has built up its full time staff from two to five FTE. Each Incubatee has an assigned investment manager with whom they work on a daily basis. Epicorp has a flexible investment model. It provides seed funding to Incubatees in return for equity. Incubatees can pay a small annual charge to participate in Epicorp’s incubation program or provide an additional small amount of equity instead. Epicorp charges commercial rent for space occupied by Incubatees.

Its Incubatees can choose to use professional services from any provider based on their business needs. They can also choose from any of the professional service firms with which Epicorp has special arrangements. Some professional services are provided by Epicorp as part of its incubation program.

Epicorp offer two levels of incubation. Stage 1 Incubatees receive less than \$50,000 in investment and stay with Epicorp for an average of 3 months. Graduation is achieved at the completion of a structured business development program provided in-house and spread over three months. The ACT Government and the Incubatee both contribute to the cost of participation.

Graduates from Stage 1 may be accepted for full incubation, which usually involves investment of more than \$50,000, and takes 18 months on average. Graduation is defined as the achievement of jointly defined performance indicators such as a corporate structure, marketing plan, business/strategic plan, satisfactory governance arrangements, an appropriate management team and channel partners.

Epicorp sources most of its Incubatees through ICT industry contacts or networks and is increasing the number sourced from CSIRO and other research institutions.

Epicorp reports that it has met or exceeded the milestones in its original agreement with the Australian Government. These milestones included admitting and graduating a number of start-up companies across the grant period and achieving sustainable business operations.

Epicorp has accepted 26 companies (14 received less than \$50,000 investment and 12 received more than \$50,000) and graduated 11 companies (7 which had received less than \$50,000 and 4 that had received more than \$50,000) up to 30 June 2003. Some 8 of its graduates (5 that had received less than \$50,000 and 3 that had received more than \$50,000) are still trading. It plans to continue to accept companies over the remaining grant period.

### ***Financial Information***

Epicorp received \$6.6m of its \$8m BITS allocation up to 30 June 2003. Some 76 per cent of the \$5m of funds expended to 30 June 2003 was provided to Incubatees as cash investment. Epicorp estimates that it has leveraged:

- significant in-kind support from a variety of sources, which the evaluation team has estimated at about \$0.9m;
- other financial contributions of \$2.2m, most of which came from ACT Government sources; and
- additional investment (received by its Incubatees) of \$10.1m that it had a facilitating role in, around half of which came from venture capitalists and business angels and the other half from state government sources.

Epicorp estimates that its initial application for BITS funding cost \$100,000 to prepare and that it has spent about \$50,000 in meeting reporting and other DCITA requirements.

Incubator set up costs were estimated at around \$915,000 with the major impost being in respect of fit out costs (81 per cent) and office equipment (14 per cent). Running costs averaged around \$627,000 per year over the last three years, with average payroll costs accounting for 16 per cent of BITS funding received.

The average rate of equity it takes in its Incubatees is 17 per cent, although it has taken equity rates in its Incubatees as low as 1 per cent and as high as 30 per cent. To 30 June 2003, Epicorp had one investment exit through a trade sale which realised \$40,000.

Epicorp reports that its Incubatees have achieved the following outcomes to 30 June 2003.

- Employment has risen from 56 to 70 FTE.
- Total revenue has risen from \$720,530 to \$2.4m.
- Total export revenue has risen from \$441,000 to \$1.6m.

### **Quality Factors**

Epicorp's management team appears to have the relevant expertise and skills necessary for working effectively with Incubatees. Epicorp's management team meet weekly to review progress. Epicorp's governance structure appears larger and more complex than other Incubators. This may be a function of its original design, which involves a separate seed fund with trustees. Epicorp has an investment committee that reviews proposals.

It also appears to have developed an appropriate array of formal and informal assistance arrangements with professional service providers to assist its Incubatees.

Other in-house services provided by Epicorp to its Incubatees include:

- advice with business planning;
- financial management advice;
- a mentoring program;
- marketing and sales services;
- secretarial services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

Epicorp has obtained the services of a large group of mentors who are involved with Incubatees by mutual agreement and operate on a *pro bono* basis.

It has 670 square metres of space available for resident Incubatees, which equates to around 72.5 square metres per Incubatee plus a common space. Epicorp facilities include office services and equipment, server and LAN facilities plus high speed Internet access. Epicorp has enjoyed high occupancy rates and has been able to achieve some synergies between Incubatees.

Epicorp has developed a close relationship with some investment funds and has established a business angel network. Originally promised involvement of two venture capital funds did not transpire.

Epicorp scored very well against the quality criteria set out in Table 2.1.

### **Comments by Incubatees**

Some 67 per cent of Epicorp's Incubatees that received significant assistance and 14 per cent that received limited assistance responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) either very good or excellent.

Although only a very small proportion of BITS funding was delivered by Epicorp as in-kind services on a charge back basis, all the Incubatee respondents to the questionnaire that actually received these services commented that they thought that they represented value for money.

A majority of the comments received from Epicorp's Incubatees were positive, for example:

Networking/advice/services all very good and difficult to get elsewhere.

Strengths: good people, supportive environment, excellent advice, good premises, fine mentoring environment and experienced board member.

Epicorp Incubatees

One Incubatee commented on the problem of filling the funding gap sufficiently so that next stage financiers will be interested in investing in BITS supported businesses.

Weaknesses: BITS Program and Incubatees don't seem to have requisite respect from financiers and venture capitalists; higher level networking could be done.

Epicorp Incubatees

### ***Epicorp's Perspective***

Epicorp management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

Epicorp expects that it could maintain its activities at or near current levels beyond 30 June 2004 for approximately six months, although Incubator activities would need to be reduced significantly after that time. It would require further funding and would take more than 12 months to be viable.

It notes that continued ability to provide equity seed funds is totally dependent on achieving financial exits and/or further funding being provided.

### ***Overall Assessment***

Epicorp has been very successful when the small Canberra ICT base and the lack of local venture capital are taken into account. Epicorp has managed to overcome these challenges with its mentor and business angel networks. These achievements reflect the strength of Epicorp's management. Epicorp's Incubatees appreciate the value which the Incubator has added. Epicorp's strong working relationship with the ACT Government is also a commendable feature.

## **3.7 Information City Victoria — Victoria**

### ***Introduction***

Information City Victoria (ICV) is a for-profit, mixed Incubator (physical and virtual) based in the Melbourne CBD. Since commencing operations, ICV has slowly built up its full time staff from five to seven FTE. Its investment model is a blend, where Incubatees are provided with a mix of cash (17 per cent) and services (83 per cent).

Its Incubatees are able to choose ICV's own professional service providers, or to select from any of the professional service firms with which ICV has special arrangements.

Incubatees that receive less than \$50,000 in investment stay with ICV for an average of 1 to 3 months, whereas those that receive more than \$50,000 in investment stay with ICV for an average of 12 to 18 months. Graduation is achieved at the end of the Incubator agreement and when external funding support has been achieved and/or the business is sustainable from sales.

ICV sources most of its Incubatees through industry contacts or networks and is increasingly creating deals through its mentor program focussed on commercialising public sector research.

ICV has accepted 44 companies (11 that received less than \$50,000 and 33 that received more than \$50,000) and graduated 10 companies (one that received less than \$50,000 and 9 that had received more than \$50,000) up to 30 June 2003. Nine of its graduates are still trading (one that had received less than \$50,000 and eight that had received more than \$50,000).

### ***Financial Information***

ICV received nearly \$7.3m of its \$8.8m BITS allocation up to 30 June 2003, 13 per cent of which was given to Incubatees in cash. ICV estimates that it has leveraged:

- in-kind contributions valued at \$3m, 10 per cent of which have been provided to its Incubatees;
- other financial contributions of \$910,000, most of which have been received from shareholders/guarantors; and
- additional investment (received by its Incubatees) of \$1.4m that it had a facilitating role in, most from business angels (the early departure of one of ICV's original investors left the Incubator without its planned source of investment funds).

ICV estimates that it incurred \$200,000 in costs in its initial application for BITS funding and \$40,000 in costs in meeting reporting and other DCITA requirements.

Set up costs were estimated at \$1m with the major impost being in respect of office equipment costs (37 per cent). Running costs averaged around \$670,000 per year over the last three years, with average payroll costs accounting for 14 per cent of BITS funding received. The majority of payroll costs relate directly to the provision of advisory and business development services to Incubatee companies.

The average rate of equity ICV takes in its Incubatees is 15 per cent, although it has taken equity rates as low as 3 per cent and as high as 45 per cent.

To 30 June 2003, ICV has had no investment exits or trade sales and has had one write off.

ICV reports that its Incubatees have achieved the following outcomes to 30 June 2003.

- Employment has risen from 32 to 35 FTE.
- Total revenue has risen from \$140,000 to \$1,105,407.
- Total export revenue has risen from \$50,000 to \$248,000.

### ***Quality Factors***

ICV has set up an independent marketing and technical assessment panel for each investment that it makes.

ICV is minimising its external risk by creating revenue sources through a number of profit centres. These include revenue in respect of incubator services to Incubatees, business plan software (developed in-house), a management fee and other sources of external funding.

ICV has a network of external professional service providers that includes accountants and legal advisors. Its Incubatees can access these and receive a lower negotiated price that is usually fixed.

Prospective Incubatees are given assistance with the development of a business plan.

ICV's Incubatees graduate when they complete their prescribed program and they are financially self-sustaining.

ICV has an occupancy rate of 80 per cent. It aims to get a mix of shorter and longer stay businesses. It changes the amount of rent that its Incubatees pay as they progress as a form of market discipline. This occupancy rate has recently reduced however as a direct reflection of the mentor program, which primarily involves one external Entrepreneur Manager acting as CEO for the Incubatee company.

ICV's management team appears to have relevant expertise and skills capable of working effectively with Incubatees.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers an in-house, formal business development training program to its Incubatees, as well as other occasional training sessions.

Other in-house services provided by ICV to its Incubatees include:

- advice with business planning;
- financial management advice;
- marketing and sales services;
- secretarial services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

It has 600 square metres of space available for resident Incubatees, which equates to around 10 square metres per Incubatee including common space (meeting rooms, café etc). ICV facilities include office services and equipment, server and LAN facilities plus high speed Internet access. It also provides workshop facilities.

ICV has developed a close relationship with an investment fund.

#### ***Comments by Incubatees***

Some 29 per cent of ICV's Incubatees that received significant assistance and 83 per cent that received limited assistance responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) either good or very good.

Only half of ICV Incubatee respondents to the questionnaire commented that they thought that the in-kind services provided by ICV's on a charge back basis represented value for money. Of the respondents that questioned the value for money, most felt they could have sourced the services themselves at a lower price, in particular, rent and other services such as Internet access. As one Incubatee commented:

I believe I could have sourced the services myself at a better rate than what was offered.

ICV Incubatee

The comments received from ICV's Incubatees were mixed. Most were happy with the access that was provided to quality advisors and the quality of the mentoring services. On the other hand, most commented that they would have liked more cash assistance and more flexibility in spending the cash. The following comments by ICV Incubatees highlight some of the strengths of ICV's program.

ICV provided access to quality advisors and a network which opens doors across Melbourne's business community.

The incubator gave me an opportunity to further develop my business plan and seek advice from people with specific experience.

ICV Incubatee

### ***Information City's Perspective***

Information City management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

It has a strong systems-based ASP management system (Information City Systems – SYNC). It also runs its mentor program, in which experienced entrepreneurs are used to build public and private sector research into businesses (for instance, RMIT, Peter MacCallum Cancer Centre).

It believes that the Victorian market is a potentially large one, and it is more constrained by the challenge of building relationships with public and private R&D organisations.

Information City has been able to convince the local business community to contribute to its operation in a number of ways. The Melbourne City Council contributed \$200,000 for a fitout and Ericsson donated several thousand dollars worth of communications equipment. Sun Microsystems also contributed \$500,000 in computer equipment.

### ***Overall Assessment***

ICV has taken a somewhat different approach to most of the other Incubators. It has put considerable effort into business training and in creating other sources of revenue for the Incubator. It has been willing to assist companies whose prospects are more modest, but are nevertheless capable of growing to be at the very least, self sustaining, profitable enterprises.

The early departure of one of the founding groups of ICV was a set back from which they rapidly recovered. However, the loss of this group left ICV without the close relationship with a source of investment funds.

### **3.8 InQbator – Queensland**

#### ***Introduction***

InQbator is a for-profit, mixed Incubator (physical and virtual) based in the Varsity Lakes technology precinct at Robina on the Gold Coast in Queensland. It is owned by its management. Since it opened its doors, InQbator has slowly built up its full time staff from three to five FTE and has plans to soon expand this to six.

InQbator's investment model is a blend, where Incubatees are provided with a mix of cash and services, although the services are not provided on a charge back basis. InQbator characterises the model it operates under as a 'sweat equity' model — that is, the equity is earned by the value added provided in the incubation process. InQbator maximises the resources invested in Incubatees and operates on relatively low overheads and running costs. InQbator's founders claim that they will benefit only if and when their investments pay off.

InQbator's Incubatees are able to choose their own professional service providers, or to select from any of the (approximately) 25 professional service firms with which InQbator has special arrangements.

Incubatees stay with InQbator for an average of 18 months and graduation is achieved at the end of the Incubator agreement. InQbator sources most of its Incubatees through industry contacts or networks.

InQbator has accepted 12 companies and graduated five companies up to 30 June 2003. Eleven out of its 12 companies are still trading.

#### ***Financial Information***

Up to 30 June 2003, InQbator had received \$7.4m of its \$9.5m BITS allocation, 90 per cent of which had been given to Incubatees in cash. InQbator estimates that it has leveraged:

- in-kind contributions valued at (at least) \$1.78m, 80 per cent of which have been provided to its Incubatees;
- other financial contributions of \$1.06m (including substantial non-equity capital contributions and an ancillary program funded by the Gold Coast local government to advise 'near miss' applicants); and
- additional investment (received by its Incubatees) of \$7.75m that it facilitated. This includes business angel investment, venture capital and funding from other State and Commonwealth Government programs. The Commonwealth programs include COMET, BIF, a Networking the Nation grant and other grants from DAFF and DITR. Its major fund-raising success was in relation to Genetraks, where InQbator co-invested with ADI. Genetraks is a Brisbane-based bioinformatics company that was successful in raising over \$7.6m in venture capital.

InQbator believes that it has strong brand awareness in the Gold Coast and South East Queensland area and has been able to achieve strong support from professional services firms in terms of discounted services to its Incubatees. It also has benefited from the support of a local technology park development. InQbator's Incubatees receive strong support from a network of mentors, whose services are available free-of-charge to the Incubatees.

InQbator estimates that it incurred \$50,000 in costs in its initial application for BITS funding and \$100,000 in costs in meeting reporting and other DCITA requirements.

Set up costs are estimated at \$218,000 with the major impost being in respect of fit out costs (62 per cent). Running costs averaged around \$366,000 per year over the last three years, with average payroll costs accounting for 12 per cent of the BITS funds received.

The average rate of equity it takes in its Incubatees is 20 per cent, although it has taken equity rates in its Incubatees as low as 5 per cent and as high as 39 per cent. It expects that its equity in Incubatees will be diluted over time to around 10 to 12 per cent.

To 30 June 2003, InQbator has made no investment exits, although it had one partial trade sale which returned \$800,000 and one write off. Two of its Incubatees are currently proposing to merge.

InQbator encourages many of its Incubatees to outsource their labour requirements. As a consequence, increases in direct employment understate the full impact of InQbator's assistance. InQbator reports that its Incubatees have achieved the following outcomes to 30 June 2003.

- Employment has risen from 14 to 69 FTE, although it encourages its Incubatees to outsource labour as much as possible to reduce costs.
- Total revenue has risen from \$1.8m to \$5.6m.
- Export revenue has risen from zero to \$49,000.

### ***Quality Factors***

Because InQbator is owned by its management, its Board comprises the management team. InQbator does have a broadly based external Advisory Board that acts like an investment and compliance committee. The external Advisory Board meets with management three to four times a year. The Board operates under a code of corporate governance and ethics.

InQbator's management team has relevant expertise and skills needed to work effectively with Incubatees. It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers an outsourced, formal business development training program to its Incubatees, and informal business training is provided in-house.

Other in-house services provided by InQbator to its Incubatees include:

- advice with business planning;
- financial management advice;
- a mentoring program;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

InQbator has 250 square metres of space available for resident Incubatees, which equates to around 30 square meters per Incubatee, plus common space. InQbator facilities include office services and equipment, server and LAN facilities plus high speed Internet access. It also has negotiated access to office space interstate and provides Incubatee access to Gartner research reports/advice and data.

While InQbator has developed a close relationship with an investment fund, it still shops around on a case-by-case basis for the best investment deals it can find.

InQbator operates from attractive premises that are well located and suited to the Incubator operation. InQbator's business strategy appears well founded and the management is selective in targeting Incubatees. InQbator's links with services providers are strong and advantageous to its Incubatees.

### ***Comments by Incubatees***

Some 80 per cent of InQbator's Incubatees responded to the questionnaire. A clear majority of comments received about InQbator from its Incubatees were positive — there were only a few critical comments and these were qualified and constructive.

None claimed that the range of services provided by or through InQbator should be changed, although a greater focus on corporate coaching was suggested as an area that could be improved. All respondents reported that the assistance provided by InQbator management represented value for money. Incubatees universally praised the value of advice provided as being of a very high standard. Most respondents rated its performance in respect of the services they received as being (on average) either very good or excellent.

A clear majority of comments received about InQbator from its Incubatees were positive – there were only a few critical comments and these were qualified and constructive. The following comments by InQbator's Incubatees summarise its standing with its clients.

Great team. Well connected. Excellent contribution to board meetings. Available for advice. Minimum bureaucracy.

The greatest value lies in breaching the 'start of the investment gap' with potential commercial investors/VCs. The difficulty in sourcing initial capital funding in Australia remains extreme, even for experienced management teams.

InQbator Incubatees

### ***InQbator's Perspective***

InQbator management is of the view that the business has progressed at about the rate it was expected to at the start of the grant period. While it acknowledges the changed investment climate due to the so-called 'tech wreck', it claims that its investment model is robust enough to be successful in spite of this. It believes that when the BITS Program was conceived the model made 'good sense', although now that the availability of venture capital has decreased, the time required for Incubators to become profitable has lengthened considerably.

InQbator believes that its key value adding is to shorten the path from idea to market. It believes it will be ultimately successful if in the meantime its investee companies remain viable, are capable of responding to changes in their environment, and do not fail. It also claims to have a class of investment or asset managers that have earned their credibility with later stage investors – that is, it has filled a gap in the investment market.

It claims that its strengths include being a low cost operation, having a measured investment rate, good utilization of business networks, commercial experience, and having reputational credibility in marketplace. It claims that the weaknesses of its operation to date lie in having insufficient operational resources and critical mass.

InQbator considers that the quality of professional services available on the Gold Coast is high. It has been able to source good quality deal flow from local, regional and interstate sources. It believes, however, that the co-investment and follow on investment pool in its region is small and difficult to mobilise and that there is little venture capital investment activity in Queensland and little organised private equity, but this is being changed gradually through an ‘advisors’ network.

InQbator expects that it could maintain its activities at or near current levels beyond 30 June 2004, although it would require further funding and would take at least 12 months to be viable. It notes the risk that some of its Incubatees could be ‘left high and dry’ if the BITS funding were to conclude on 30 June 2004. InQbator believes that in the medium term there is space for probably only three or four successful IT Incubators in Australia.

### ***Overall Assessment***

InQbator’s investment model is a good example of how an Incubator can be operated. InQbator ensures that the majority of government funds are actually received by the Incubatees. By running the business with low overheads and aligning the payoff to management with the success of its investments, it sends a signal that it is willing to shoulder a good deal of the risk that would otherwise be taken on almost exclusively by the government.

The principle it operates under is that if the investments do not pay off, management does not benefit. Similarly, in order for management to benefit, the investments have to pay off. This is unlike some other models, where management is paid market rates from day one with the prospect of even further reward when (and if) investments are realised.

InQbator scored very well against the quality criteria set out in Table 2.1.

### **3.9 In-tellinc Pty Ltd – Tasmania**

#### ***Introduction***

In-tellinc is a for-profit, mixed Incubator (physical and virtual) based in Hobart and servicing all of Tasmania. The In-tellinc consortium comprises IItem3 (a Sydney-based BITS Incubator), KPMG and University of Tasmania. The In-tellinc Incubator shares many common features with incubators funded under the BITS Incubator Program and has therefore been included in this evaluation. Since it began trading, In-tellinc has gradually built up its full time staff to five FTEs. Its investment model is a blend, where Incubatees are provided with a mix of typically cash (33 per cent) and services (67 per cent).

Its Incubatees are able to choose In-tellinc's own professional service providers, or to select from any of the professional service firms with which In-tellinc has special arrangements.

Incubatees stay with In-tellinc for an average of 18 to 24 months and graduation is achieved through either self sustaining funding, third party follow on funding or a trade sale or listing. In-tellinc sources most of its Incubatees through ICT industry contacts and networks.

In-tellinc has accepted 12 companies and graduated 1 company up to 30 June 2003. Its only graduate is still trading and 11 out of its 12 companies are generating revenue.

#### ***Financial Information***

In-tellinc received \$6.3m of its \$8m BITS allocation up to 30 June 2003, 20 per cent of which was given to Incubatees in cash. In-tellinc estimates that it has leveraged:

- in-kind contributions valued at around \$420,000, 15 per cent of which have been provided to its Incubatees;
- other financial contributions of \$759,000, most of which has been received from Sun Microsystems; and
- additional investment (received by its Incubatees) of \$2.4m that it had a facilitating role in, most of which was provided by business angels.

In-tellinc Pty Ltd estimates that it incurred \$187,000 in costs in its initial application for BITS funding and \$74,000 in costs in meeting reporting and other compliance requirements.

Set up costs were estimated at \$363,000 with the major impost being in respect of other setting-up costs (84 per cent). Running costs averaged around \$694,000 per year over the last two years, with average payroll costs accounting for 10 per cent of the BITS funds received.

The average rate of equity it takes in its Incubatees is 25 per cent, although it has taken equity rates in its Incubatees as low as 8 per cent and as high as 40 per cent.

To 30 June 2003, In-tellinc has had no investment exits and no trade sales.

In-tellinc Pty Ltd claims that its Incubatees have achieved the following outcomes to 30 June 2003:

- Employment has risen from 19 to 49 FTE.
- Total revenue has risen from \$239,000 to \$3.5m.
- Total export revenue has risen from \$174,000 to \$1.73m.

### **Quality Factors**

Like most of the regional Incubators, In-tellinc has a high profile with the local business community, the State Government and local universities. A representative from the Tasmanian Government advised that In-tellinc has had an impact on State Government policy and that the Government endeavours to assist with deal flow through its other programs that encourage and assist small businesses. In this regard, it was noted that around half of In-tellinc's Incubatees had been participants in Tasmanian Government training programs.

In-tellinc appears to have been successful in working in with various local and national initiatives. Close relationships have been established with the Tasmanian State Government, Intelligent Island Program, Tasmanian Electronic Commerce Centre, Tas IT, Tasmanian Information Technology Industry Council, University of Tasmania, Sun Microsystems and EDS.

Prospective Incubatees are given assistance with the development of a high level business plan that forms the basis of In-tellinc investment.

In-tellinc's management team appears to have relevant expertise and skills capable of working effectively with Incubatees.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It offers an outsourced, formal business development training program to its Incubatees, and informal business training is provided in-house.

Other in-house services provided by In-tellinc to its Incubatees include:

- active development and delivery of business and sales and marketing plans;
- financial management advice and accounting services;
- legal and commercial assistance;
- accounting services;
- marketing and sales services;
- secretarial services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

In-tellinc has 240 square metres of space available for resident Incubatees, which equates to around 30 square metres per Incubatee plus a common space and meeting/Board rooms. In-tellinc facilities include office equipment, CD production, server and LAN facilities plus high speed Internet access.

While In-tellinc has developed a relationship with an investment fund, it still shops around on a case-by-case basis for the best investment deals it can find.

### ***Comments by Incubatees***

All of In-tellinc's Incubatees responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) either very good or excellent.

Nearly all of Incubatee respondents to the questionnaire commented that they thought that the in-kind services provided by In-tellinc on a charge back basis represented value for money.

A majority of the comments received from In-tellinc Incubatees were positive. The following comments highlight the quality of the In-tellinc operation.

Strengths: opportunities to cluster pools of dynamic companies with similar requirements that can share and cross pollinate ideas and resources. Weaknesses: Business managers need to communicate more with other incubators to broaden knowledge, contacts and networks.

Strengths: commercialisation experience of incubator board member provides conduit to additional funding opportunities and assistance with funding application.

In-tellinc Incubatees

### ***In-tellinc Perspective***

In-tellinc's management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

It believes that its strengths lie in it providing a hands-on assistance incubation model, run by managers with practical commercial experience. It also sees the breadth and depth of its networks as being a key strength. Weaknesses listed by In-tellinc include the limited size and scale of the operation and its inability to provide a full incubation program with constant funding.

In terms of its regional location, In-tellinc believes that its remoteness creates an extra challenge to creation of channels to market and sales. In addition, the small size and scale of the Tasmanian market makes it difficult, and success usually has to be based on interstate sales.

In-tellinc claims that Government/Intelligent Island support for the Incubator has been good with various pieces of funding for In-tellinc and Incubatees. Shareholder support has been very good with heavily discounted or free services. The business community, more generally, had provided very limited support.

### ***Overall Assessment***

In-tellinc has done remarkably well in the short time it has been operating, particularly given its relatively remote location and small size of the Tasmanian ICT market. In-tellinc has made a genuine effort to include Incubatees from all over Tasmania and has been effective in engaging the State Government in a strong working relationship. In-tellinc received positive comments from all its Incubatees in relation to the survey question regarding value for money in respect of the in-kind services it provided on a charge back basis. In-tellinc Incubatees are achieving encouraging results and are achieving a good rate of commercialisation with good revenue growth.

### **3.10 IItem3 Pty Limited – New South Wales**

#### ***Introduction***

IItem3 is a for-profit, mixed Incubator (physical and virtual) based in Sydney. It sought to address innovation market failure by investing in very early stage technology companies, the majority being late R&D/pre-revenue entities. Since it opened its doors, IItem3 retained a core of 3 FTE with up to 8 FTE at peak operation. Its investment model is a blend, where Incubatees are provided with a mix of cash (33 per cent) and services (67 per cent).

Its Incubatees work with IItem3's own business managers and select from a range of professional service firms with which IItem3 has special arrangements.

Incubatees stay with IItem3 for an average of over 24 months and graduation is achieved when Incubatees attract follow on investment, achieve self-sustaining revenue, or have a trade sale in progress. IItem3 sources most of its Incubatees through ICT industry contacts or networks.

IItem3 has accepted 11 companies and graduated three companies up to 30 June 2003. Nine of its companies (including its three graduates) are now trading. IItem3 would prefer not to take in further Incubatees during 2003-04 but instead to concentrate on providing additional assistance to existing Incubatees in order to get them to the point where they are self sustaining.

IItem3 would also like the upper limit on funds invested in individual Incubatees raised on the basis that the gap between the present limit and the point at which venture capital might be available is too wide.

#### ***Financial Information***

IItem3 received the majority of its \$7.37m BITS allocation up to 30 June 2003, 56 per cent of which was allocated to Incubatees (one third as cash investment and two thirds as services). IItem3 estimates that it has leveraged:

- in-kind contributions valued at \$475,000, 20 per cent of which have been provided to its Incubatees.
- other financial contributions of \$1.2m, most of which has been received from shareholders; and
- additional investment (received by its Incubatees) of \$3.2m that it had a facilitating role in, most of which came from business angels.

IItem3 estimates that it incurred \$104,000 in costs in its initial application for BITS funding and \$381,000 in costs in meeting reporting and other DCITA requirements.

Set up costs were estimated at \$307,000 with the major imposts being in respect of initial staff recruitment costs (39 per cent) and the preparation of legal documents (23 per cent). Running costs averaged around \$1.1m per year over the last three years, with average payroll costs accounting for 22 per cent of BITS funding received.

The average rate of equity IItem3 takes in its Incubatees is 27.5 per cent, although it has taken equity rates as low as 5 per cent and as high as 45 per cent. To 30 June 2003, IItem3 has had no investment exits, no trade sales and one write off.

IItem3 reports that its Incubatees have achieved the following outcomes to 30 June 2003.

- Employment has risen from 25 to 42 FTE.
- Total revenue has risen from \$618,000 to \$3.7m.
- Total export revenue has risen from \$360,000 to \$1.3m.

### ***Quality Factors***

IItem3's management team appears to have relevant expertise and skills capable of working effectively with Incubatees, particularly in the formative stages.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It does not offer a formal business development training program to its Incubatees, but focuses on as-needed business development training.

Other in-house services provided by IItem3 to its Incubatees include:

- advice with business planning;
- marketing and sales services;
- secretarial services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

IItem3 has 175 square metres of space available for resident Incubatees, which equates to around 8 square metres per Incubatee plus a common space. IItem3 facilities include office services and equipment, server and LAN facilities plus high speed Internet access.

IItem3 has developed a close relationship with an investment fund. However, IItem3 reports that the lack of private investment capital has been a major problem, especially given that ICT development is often capital intensive.

In addition, because the established ICT sector is under pressure, it is not buying products or services from smaller ICT companies. These factors, together with the suspension of the Government's R&D START Program for a period, have limited IItem3's scope to get Incubatees to the point where satisfactory exits can be achieved.

### ***Comments by Incubatees***

Some 45 per cent of IItem3's Incubatees responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) good.

A majority of Incubatee respondents to the questionnaire commented that they thought that the in-kind services provided by IItem3 on a charge back basis did not represent value for money.

The comments received from IItem3 Incubatees were mixed. While some noted the supportive environment provided and the usefulness of the funds provided, others commented that the facilities were too expensive and that they had insufficient control over the cash available. Others perceived that their incubation experience could have been improved if the relevant investment managers had a specific expertise in their technology field. External mentors were appointed in a number of cases. Interviews conducted by IItem3 independent Directors, revealed that expectations of the investee founders rose during the time of incubation. IItem3 regards this outcome as positive because it demonstrates increased awareness of the complex commercialisation process.

The following comments by IItem3 Incubatees highlight some of the strengths and weaknesses of the Incubator

Our company wouldn't have gotten this far without incubation. The facilities provided were top class, however, in hindsight we would have survived longer if we had used lower class, cheaper, facilities and services.

Key strengths include good corporate governance and general management mentoring. Weaknesses include low networking opportunities within investment community and inexperience in sales/marketing.

IItem3 Incubatees

### ***IItem3's Perspective***

IItem3 management is of the view that the business has not progressed at the rate it thought it would at the start of the Grant Deed. In particular, receding capital markets and the downturn in the IT industry have impacted both on the availability of capital for incubator and Incubatees alike, slowed sales and resulted in a shortage of trade sale prospects. A number of venture capital providers commented that they could not invest in IItem3, perceiving it as a 'fund' rather than an operating business.

IItem3 expects that its activities would require further funding and need more than another two years funding beyond 30 June 2004 to be viable. It notes that recovery in the IT sector is critical to the success of the BITS Incubators.

IItem3 believes that its strengths lie in its ability to capture new technologies and develop businesses from them and that BITS provides a public sector R&D commercialisation alternative to licensing. It also believes that its strength has been to systematise Angel Investment in small ICT start-ups. IItem3 notes the weaknesses of its operation are that it is capital and labour intensive.

IItem3 notes that the business community has provided assistance in the form of *pro bono* work on its advisory committee and bulk purchase rates from selected service providers.

### **Overall Assessment**

ITem3 has a strong Board but was not able to make a successful exit and thus generate revenue for ongoing operations. It was also not able to obtain support from the NSW State Government. In the Sydney market where there is some investment capital, it was not successful in raising significant amounts for its very early stage Incubatees.

### **3.11 Original IT Investments (OIT) – Darwin**

#### **Introduction**

OIT is a for-profit, physical Incubator based in Darwin in the Northern Territory. OIT has employed up to four FTE Incubator staff and had two FTE staff as at 30 June 2003. Since the departure of a business and a marketing adviser these services have been outsourced.

Its investment model involves the provision of cash to Incubatees, who then purchase services and, for those located in the Incubator, pay rent. OIT's Incubatees have received assistance from professional services providers with whom OIT has special arrangements.

OIT sees incubation as involving four levels.

1. Due diligence.
2. Proof of concept.
3. Market ready company.
4. Commercialisation.

Incubatees stay with OIT for an average of 18 months and graduation is achieved when Incubatees reach its Level 3. At this level, the Incubatee has a business plan, a market ready product and the Incubatee is a fully operational company with initial sales having been achieved.

OIT sources most of its Incubatees through industry contacts or networks. Outsourcing the NT Government's computer services in 1999 contributed to a contraction of the ICT industry in the Territory with many ICT professionals leaving Darwin. OIT reports that its deal flow has been limited. OIT has not accepted some potential Incubatees because it was not confident that it could complete incubation and achieve an exit within the time period of the BITS grant.

OIT continues to follow its original strategy, although it has not achieved the targeted numbers of Incubatees and the proposed level of co-investment. The exits originally proposed for the year 2003-04 now seem unlikely to be achieved. OIT reports that most of its Incubatees are only now becoming 'investment ready'.

OIT has accepted 14 companies and graduated five companies up to 30 June 2003. It also had five withdrawals. Five of its graduates are still trading.

#### **Financial Information**

It received \$4.6m of its \$5m BITS allocation up to 30 June 2003, 69 per cent of which was given to Incubatees in cash. OIT estimates that it has leveraged:

- in-kind contributions valued at up to \$50,000; and
- other financial contributions of \$2.2m (largely from shareholders or guarantors).

OIT indicated that it has not been able to facilitate the raising of any additional funds in respect of its Incubatees. While a local agent represents Foundation Capital, OIT reports that there are no venture capital or business angel funds available in Darwin. Interstate investors prefer to be located closer to companies in which they invest.

OIT reports that it has ready access to professional services, organisations and senior business executives.

Set up costs were estimated by OIT at \$116,000 and running costs averaged around just under \$800,000 per year over the last three years, with average payroll costs accounting for 19 per cent of the BITS funds received. OIT estimates that it incurred \$7,000 in meeting reporting and other DCITA requirements.

The average rate of equity it takes in its Incubatees is 37.5 per cent, although it has taken equity rates in its Incubatees as low as 30 per cent and as high as 40 per cent.

In respect of commercial outcomes, OIT has not achieved any investment exits, trade sales or floats.

OIT reports that employment in its Incubatees has risen from zero to 15 FTE between the start of the grant period and 30 June 2003. OIT reported no Incubatee revenues or exports.

### ***Quality Factors***

The Board of OIT comprises a local businessman together with representatives of a local energy company, the Northern Territory University. This does not appear to provide the breadth of interest and skills seen in many of other Incubator Boards. In relation to a business development training program, OIT offers occasional sessions conducted in-house.

Other in-house services provided by OIT to its Incubatees include:

- advice with business planning;
- a mentoring program;
- secretarial services;
- networking opportunities;
- use of meeting rooms; and
- provision of a Director on the Board of Incubatee companies.

OIT's mentoring panel, comprising a Board member and OIT staff, meet with Incubatees on a monthly basis to discuss progress. Attempts to find external mentors have not been successful.

OIT has 220 square metres of space available for resident Incubatees, which equates to around 25 square metres per Incubatee plus common areas. OIT facilities include office services and equipment, server and LAN facilities plus high speed Internet access.

OIT claims that it has developed a close relationship with an investment fund — Foundation Capital in Perth, although it has yet to attract any additional funding. It approaches investment sources on a case-by-case basis. OIT also reports that it has good access to professional associations and local senior business executives.

### ***Comments by Incubatees***

Of the three people who responded to the questionnaire, two were withdrawals that were critical of OIT's performance — particularly the circumstances surrounding their respective withdrawals. The one current Incubatee that responded noted that it had 3 FTE staff and no sales. Overall, the questionnaire responses were of poor quality and gave no real insight into the kind (or quality) of assistance provided by OIT. Most respondents rated its performance in respect of the services they received as being (on average) either poor or good.

One of the two survey respondents who received in-kind services provided by OIT on a charge back basis commented that they represented value for money.

### ***OIT's Perspective***

OIT expects that its activities would need to be reduced significantly beyond 30 June 2004, and that it would require further funding and would need at least a further two years funding to be viable. In the absence of such support, OIT is likely to cease incubation activities and become a holding company for its investments.

OIT claims that its key strength (and weakness!) is that it assists very early stage companies. This is interpreted as meaning that it fills a gap in the market (strength), but that doing so is risky and difficult (weakness). It believes that it is severely limited in what it can do by virtue of the small size of the local market for IT products and services. It also believes that the small size of the population in Darwin leads to restricted R&D opportunities.

### ***Overall Assessment***

OIT has operated in a difficult market, with a small deal flow and a lack of access to business angels and venture capital. It has also had changes of CEO and key staff during the grant period. In all these circumstances, OIT has struggled to have an impact.

## **3.12 Playford Capital – South Australia**

### ***Introduction***

Playford Capital is a not-for-profit virtual Incubator based in the Adelaide central business district. Since it began trading, Playford Capital has reduced its full time staff from eleven to eight FTE. Its investment model provides BITS funds to incubatees in the form of cash. The cost of Playford's services to its Incubatees is largely met through funding from the South Australian Government.

Playford's Incubatees are able to choose the Incubator's own professional service providers, or to select from any professional service firms with which Playford Capital has special arrangements.

Incubatees stay with Playford Capital for an average of five months and graduation is achieved at the completion of investment milestones. Playford sources most of its Incubatees through ICT industry contacts or networks.

Playford Capital has accepted 17 companies and graduated 12 companies up to 30 June 2003. All 12 of its graduates are still trading.

### **Financial Information**

Playford Capital received \$7.7m of its \$10m BITS allocation up to 30 June 2003, 38 per cent of which was cash invested in Incubatees. Playford Capital estimates that it has leveraged:

- in-kind contributions valued at around \$25,000;
- other financial contributions of \$8.1m, most of which have been received from shareholders/guarantors; and
- additional investment (received by its Incubatees) of \$14.8m that it had a facilitating role in. \$6.8 m came from Business Angels and \$8m from venture capitalists.

Playford Capital estimates that it incurred \$250,000 in costs in its initial application for BITS funding and \$250,000 in costs in meeting reporting and other DCITA requirements.

As Playford had already been trading for three years, set up costs were estimated at \$12,000 with the major impost being in respect of preparation of legal documents. Running costs averaged around \$1.76m per year over the last three years,<sup>28</sup> with average payroll costs accounting for 39 per cent of the BITS funds received.<sup>29</sup>

The average rate of equity it takes in its Incubatees is 7 per cent — low by comparison with some other Incubators, although it has taken equity rates in its Incubatees as low as 1 per cent and as high as 16.7 per cent.<sup>30</sup>

To 30 June 2003, Playford Capital has had no investment exits or trade sales.

Playford Capital reports that its Incubatees have achieved the following outcomes to 30 June 2003:

- employment has risen from 143 to 150 FTE; and
- total revenue has risen from \$3.9m to \$5.1m.

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<sup>28</sup> These costs are for both management of the BITS fund and Playford's previous investment fund, plus other activities it performs for the South Australian Government.

<sup>29</sup> It should be acknowledged here that Playford does not draw its running costs from its BITS grant. The South Australian Government pays for Playford's running costs.

<sup>30</sup> This low percentage is due to Playford often co-investing with others, rather than taking a larger stake initially, then having its shareholding diluted.

### **Quality Factors**

Playford Capital's management team appears to have relevant expertise and skills capable of working effectively with Incubatees.

It also appears to have an appropriate array of formal and informal assistance in place to support the development of its Incubatees. It does not offer a formal business development training program to its Incubatees.

In-house services provided by Playford Capital to its Incubatees include:

- advice with business planning;
- financial management advice;
- legal or accounting services;
- marketing and sales services;
- networking opportunities; and
- use of meeting rooms.

As a virtual Incubator, Playford Capital does not provide physical space to its Incubatees, although it makes meeting room facilities available to its Incubatees.

Playford Capital has not developed a close relationship with any one investment fund. It notes that there are no investment funds in Adelaide that routinely invest in ICT start ups, which is why there is a market failure. It has, however, built relationships with a number of business angels and formed ties with Innovation Investment Funds (IIFs) including Foundation Capital, CM Capital and Nanyang, and Adelaide corporate advisors. It sub leases office space to Foundation Capital.

Playford scored very well against the quality criteria set out in Table 2.1.

### **Comments by Incubatees**

Some 64 per cent of Playford Capital's Incubatees that received significant assistance and 33 per cent that received limited assistance responded to the questionnaire. Most respondents rated its performance in respect of the services they received as being (on average) good.

A majority of Incubatee respondents to the questionnaire commented that they thought that the in-kind services provided by Playford Capital on a charge back basis represented value for money.

A majority of the comments received from Playford Capital's Incubatees were positive. Most commented about the high quality of the mentoring services and that investment managers were very supportive. Most also highlighted the crucial nature of the cash funding provided. The following comments are typical of the responses.

The incubation money was spent on patenting costs and as such enabled us to continue with a potentially valuable patent. Additionally, the staff at Playford have been very helpful with advice and business contacts.

Without the capital we would not be in business today. Little else has mattered. Technology companies take at least 3-5 years to work out their products, value equation for clients and cashflow positive marketing channels. They need patient capital.

Strengths: Playford provided crucial support and funding to bridge our connection to the VC investors. Once the VCs were engaged and committed, Playford then stepped back.

Playford Incubatees

### ***Playford Capital's Perspective***

Playford Capital management is of the view that the business has progressed at about the rate it thought it would at the start of the grant deed.

Playford runs a model that is deliberately aligned to that used by venture capitalists and other professional investors, allowing it to maximise co-investment and subsequent investment.

It is concerned about a lack of access to corporate advisory or business angels and a lack of follow-on venture capitalists to help it build deal flow.

Its model allows other funding programs such as COMET to be used to pay for business services. It is of the view that it has generally referred its Incubatees to the best businesses that Adelaide has to offer.

### ***Overall Assessment***

Playford Capital has performed well given the lack of investment capital in Adelaide. Funding from the South Australian Government has enabled Playford to provide more intensive assistance to its Incubatees.

## *Chapter 4*

# Performance of Incubated Companies

Information about Incubatee experience with the BITS and Intelligent Island Incubator Programs was sought through a survey of all Incubatees, Graduates and companies that have withdrawn from incubation before graduating (all referred to as 'Incubatees' in this Chapter and in Appendix A). Interviews were conducted with a sample of Incubatees from each Incubator. A total of 254 Incubatee surveys were sent out via Incubators, with 100 responses received. Thus figures reported in this Chapter are not comparable with those reported in other Chapters for the BITS and Intelligent Island Incubator Programs. This Chapter provides analysis of the results from the Incubatee survey.

In the survey, Incubatees were asked to provide details of their incubation experience, including when they started incubation, what funding and services they had received and their opinions on the benefits of incubation. The majority of Incubatees who responded to the survey had commenced incubation within the last two years, with 71 per cent starting incubation on or after July 2001. Further, 29 per cent had commenced incubation during the 2002-03 financial year. Of the 100 responses received, 36 were from graduates of the Programs and 14 respondents had withdrawn from incubation, with the most common reason for withdrawal being inadequate funding provided.

### **4.1 Funding and Services Received**

#### ***Cash Funding***

Of the 100 Incubatees who responded to the survey, 90 per cent reported receiving cash funding from their Incubator, while five per cent reporting they had not received any cash, and a further five per cent did not provide any response to the question. A total of \$18,541,284 in cash funding was provided to Incubatees who responded to the survey, an average of \$195,171 per Incubatee. Thus the survey respondents accounted for approximately 70 per cent of Program Funds allocated to 30 June 2003. A further 23 Incubatees indicated that they were still expecting further cash funding from their Incubator. The total amount still to be received was \$1,572,668, an average of \$68,376 per Incubatee.

#### ***In-kind Services***

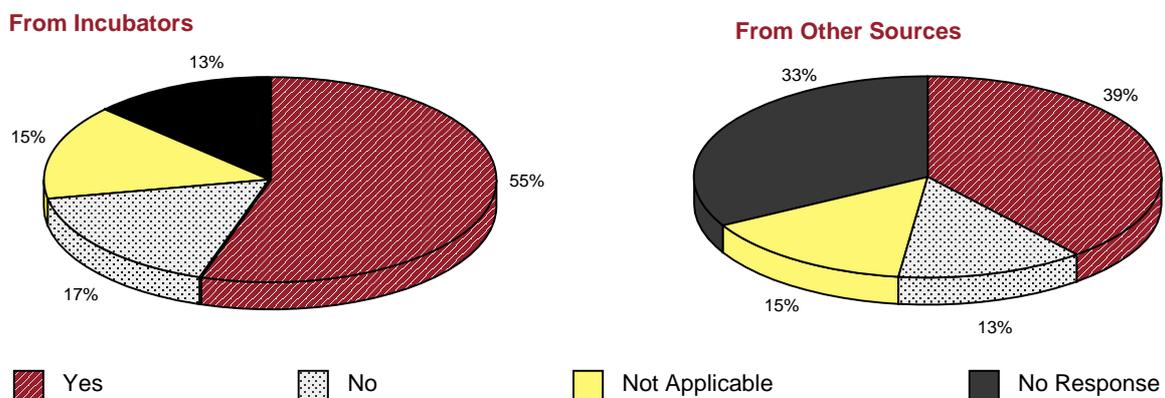
Of the Incubatees who responded to the survey, 85 per cent indicated that they had received some in-kind services from their Incubator. Of these, the majority received in-kind services with a value of less than \$50,000 (59 per cent). No Incubatee received in-kind services with a value of more than \$400,000.

Incubatees were also asked to provide details of in-kind services they received from outside sources, possibly facilitated by their Incubator. A total of 76 Incubatees reported that they had received in-kind services from sources outside of their Incubator. Again, the value of these services was relatively small, with 55 per cent of in-kind services received being valued at less than \$50,000.

Given the prominent role of in-kind services in the incubation process, particularly for certain Incubators, it is important to determine whether these services are providing Incubatees with value for money. In the survey, Incubatees were asked whether they considered that the in-kind services they received represented value for money. As shown in Figure 4.1, just over half of Incubatees who responded to the question agreed that in-kind contributions received from their Incubator represented value for money. Only 39 per cent of Incubatees agreed that they had received value for money from in-kind services received from other sources. This result must be considered with caution given the large proportion of respondents who did not provide a response to the question, with 48 per cent either not responding or indicating that the question was not applicable to them.

Figure 4.1

## VALUE FOR MONEY FOR IN-KIND SERVICES



Source: Incubatee Survey Results

While just over half of Incubatees who responded to the survey agreed that the in-kind services received from their Incubator represented value for money, a number of comments were received from Incubatees on this issue. These comments highlight concerns over lack of control and choice of in-kind services, and doubts over the value for money of the services. Several Incubatees believed that, given the choice, they could make better use of the cash value of the services.

*‘Our company wouldn’t have gotten this far without incubation. The facilities provided were top class, however, in hindsight we would have survived longer if we had used lower class, cheaper, facilities and services’.*

*‘In our case the question should be ‘would’ we have used these services if they weren’t provided by our incubator. Had the cash component of our investment not been delivered in 3 tranches we would have put up more resistance to the spending of in-kind contributions’.*

*‘I had asked what was the value of the ‘supposed’ in-kind from my Incubator, I was told those figures were not kept. They claimed in ‘conversation’ that it was valued at 180K – if I had had the 180K I would be exceeding question 18b (business progress) by 40-50%’.*

*‘I believe I could have sourced the services myself at a better rate than what was offered’.*

Other Incubatees raised concerns about the price of services provided from the Incubator, and the lack of transparency of the charges:

*‘There were no controls over what the Incubator charged for services generated in-house which were often very expensive. For example, we are paying 30% of rent we were charged by our Incubator for better accommodation and facilities.*

*‘\$200,000 of our in-kind services budget was diverted to our Incubator’s officers and employees without our control and with little apparent value and no traceability or tangible outcomes’.*

*‘Office space was expensive, Internet access was expensive’.*

Another Incubatee noted that they were not happy with being forced to pay back half of their small amount of Incubator funding (less than \$50,000) in rent to their Incubator.

### **Non-Incubator Funds Received**

A key indicator for the success of a business incubation program is the ability of Incubatees to leverage off the incubation experience and access additional funds from outside the Program. In the survey, Incubatees were asked to identify the non-BITS funds they had received, through loans, grants and equity.

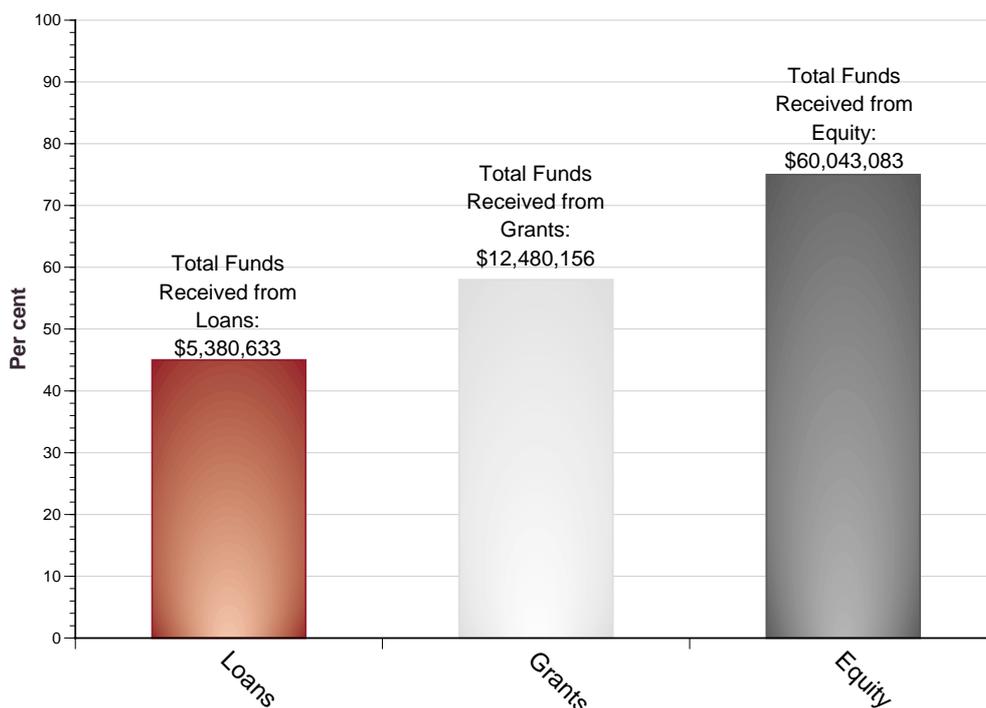
It is important to understand leverage or additionality in this regard because funds raised that would have been raised with or without the BITS and Intelligent Island Incubator Programs should not necessarily be viewed as leveraged or additional. It should be acknowledged that successful ICT start ups may be eligible to receive funds and assistance from a number of sources, including in some cases from a number of government programs. It has not been possible to estimate with any precision the proportion of non-Program funds raised purely as a result of the two Programs. While it is clear that a few Incubatees were growing businesses prior to incubation, it is equally clear that the majority owe their existence to the support provided through the Programs.

Results from the survey indicate that the largest source of funds outside of incubation for Incubatees is equity, with 75 per cent of respondents receiving funds through equity (Figure 4.2). The total value of equity raised by Incubatees who responded to the survey was just over \$60m, an average of approximately \$800,000 per Incubatee. The primary source of equity was their shareholders (32 per cent of respondents) followed by Incubatees’ own equity (27 per cent of respondents).

Grants were also an important source of funds for Incubatees, with 58 per cent of Incubatees receiving grant funding, for a total value of \$12.4m. The most common source of grant funding was the Australian Government, with 31 per cent of all grant recipients receiving an Australian Government grant. COMET grants were the most highly represented, with 11 Incubatees receiving grants from this Program, followed by R&D Start grants (six Incubatees) and Export Market Development grants (five Incubatees).

Of those Incubatees who responded to the survey, 45 per cent indicated that they had received funding through loans. The primary source of loans was identified as ‘own funds’, with 17 per cent of Incubatees taking out loans to fund their business. The total amount of loan funds reported by respondents is \$5,380,633.

Figure 4.2

**FUNDS RAISED FROM OTHER SOURCES (PER CENT OF RESPONDENTS)**

Source: Incubatee Survey Results

**4.2 Incubatee Performance**

In assessing the effectiveness of a business incubation program, a key indicator is the performance of the incubatees in the program — how successful these companies have been in developing their business and meeting their milestones. While indicators of progress are often specific in nature to the relevant business, there are broad indicators of performance which can be assessed across all companies for comparative purposes, such as revenue, employment, profits and exports.

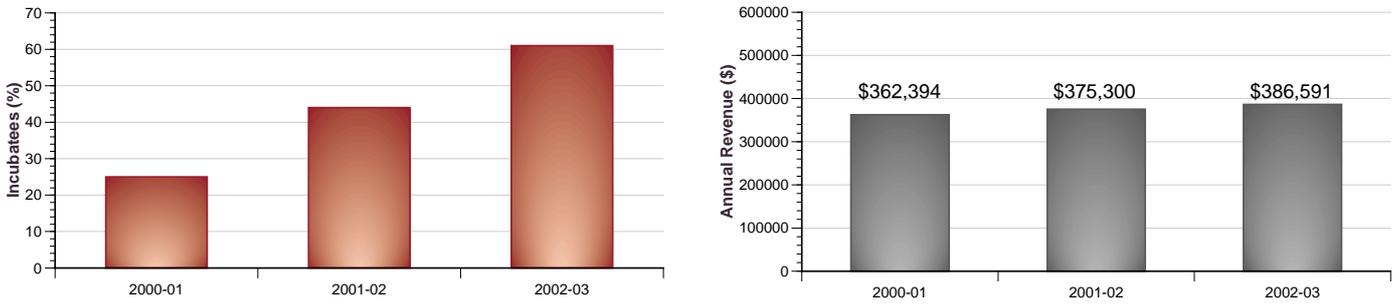
**Revenue**

In the survey, Incubatees were asked to provide details of their revenue for the last three financial years. A large number of Incubatees did not provide any response to parts of this question, most likely due to them having no revenue for the year in question. For the year 2000-01, only 25 per cent of Incubatees reported revenue, with the average for this group being \$362,394 (Figure 4.3). By 2002-03, 61 per cent of Incubatees reported revenue, with an average of \$386,591.

This result indicates that, since 2002-03, there has been significant growth in the proportion of Incubatees receiving revenue. Further, of those Incubatees who *did* report revenue in these years, the average annual revenue has increased. Therefore, not only has there been growth in the number of Incubatees receiving revenue, but also growth in the level of revenues achieved.

Figure 4.3

**INCUBATEE REVENUE, 2000-01 TO 2002-03**



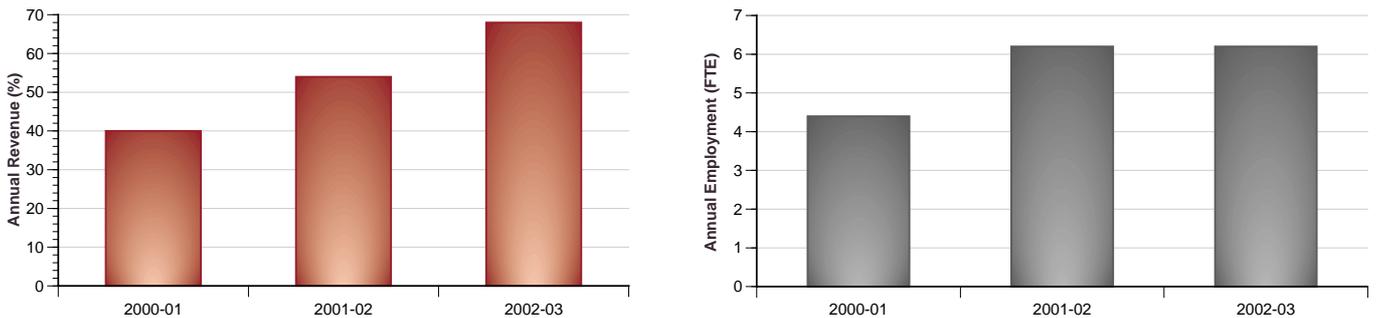
Note: Average of those who reported revenue, not of whole sample.  
 Source: Incubatee Survey results.

**Employment**

Of the Incubatees who responded to the survey, 40 per cent reported that they employed at least one Full-time Equivalent (FTE) employee in their company in 2000-01. A number of respondents reported zero employment or did not respond to the employment question in the survey. It seems likely that some company founders have not counted themselves as employees. In some other cases, companies are no longer trading. Of those Incubatees who reported employment, the average number of employees was 4.4. In 2002-03, 68 per cent of Incubatees reported employing at least one FTE employee, with the average number of employees being 6.2. As with the revenue outcomes (above), this result indicates strong growth in the number of Incubatees employing staff, and growth in the average number of staff per company, a key indicator of business growth.

Figure 4.4

**INCUBATEE EMPLOYMENT, 2000-01 TO 2002-03**



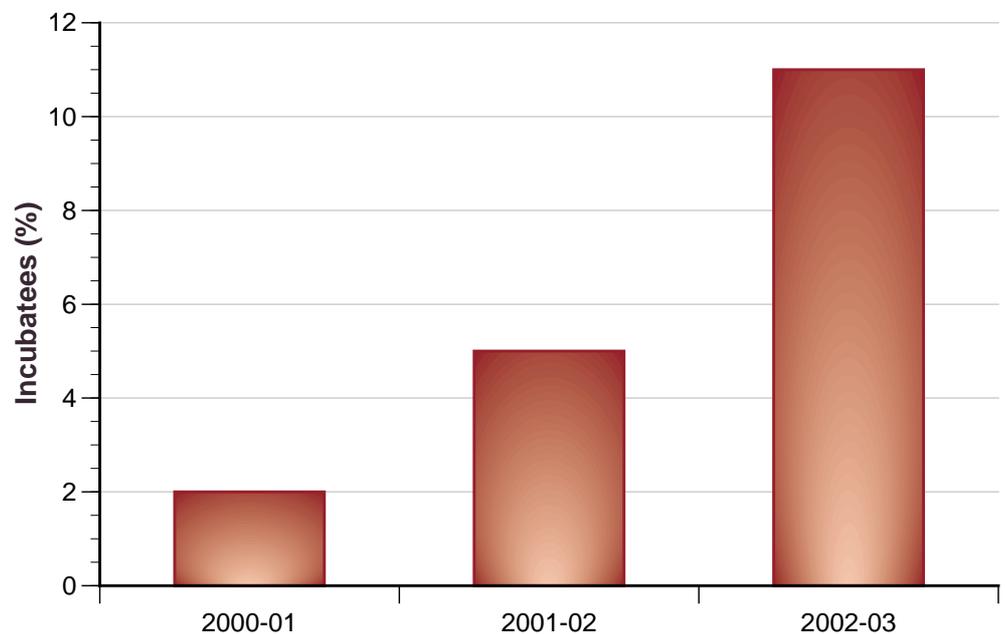
Note: Average of those who reported revenue, not of whole sample.  
 Source: Incubatee Survey results.

### Profit

Very few Incubatees reported any profit between 2000-01 and 2002-03. For 2000-01, only 2 per cent Incubatees reported a profit, with an average annual profit of \$294,000. By 2002-03, 11 per cent of Incubatees reported profits, with an average profit of \$89,997. These results indicate that there is an increasing number of Incubatees reporting profits, though the average size of the profit is falling. It is important to note here that the average profit result for 2000-01 is taken from a very small sample and is influenced by a large profit reported for one Incubatee. For 2002-03, those Incubatees who reported a profit for the first time in this year tended to report values of less than \$10,000, thus lowering the average considerably.

Figure 4.5

#### INCUBATEES REPORTING PROFITS, 2000-01 TO 2002-03 (PERCENTAGE)



Source: Incubatee Survey Results

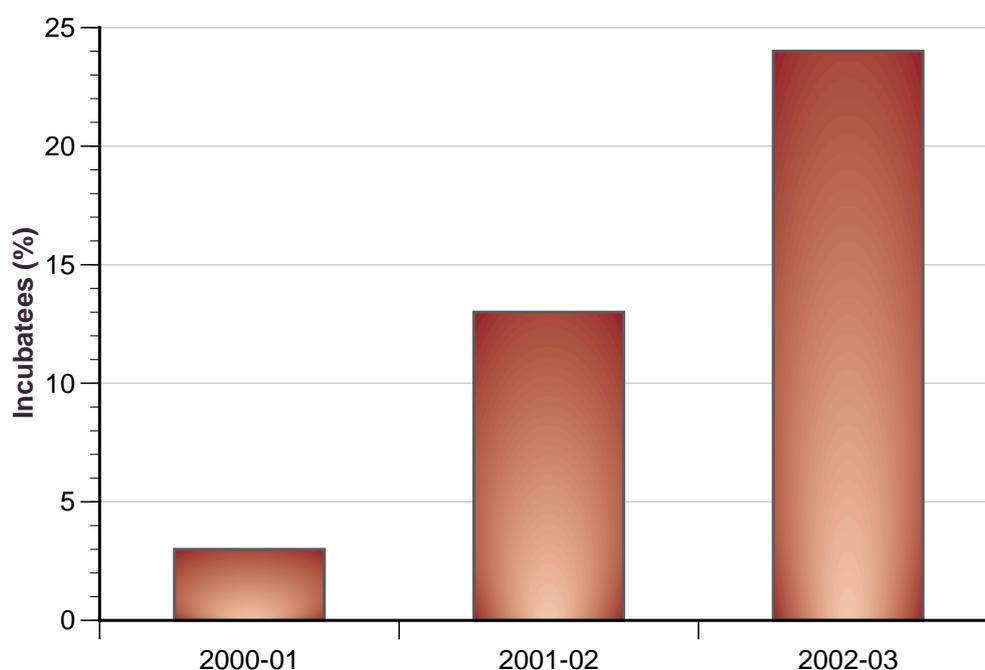
While profits are an important indicator of business progress, the measure in this case must be considered in the context of the stage of development of most Incubatee companies. These are typically companies developing new products or services and looking to invest as much capital as possible into this development process. It is likely that these companies are re-investing their revenues back into the development of the business, rather than taking profits.

### Exports

Only a small proportion of those Incubatees who responded to the survey reported revenues from exports in the last three financial years. In 2000-01, 3 per cent of Incubatees reported export revenue. By 2002-03, this proportion had increased to 24 per cent. The small proportion of Incubatees reporting export revenues in 2000-01 means the average export revenue for that year is taken from a small sample, and is influenced by a large value from one Incubatee. Hence, the average value of export revenues in 2000-01 for Incubatees is higher than for 2002-03. As with profits, in 2002-03 several companies reported export revenues for the first time at relatively low levels (six Incubatees reported export revenue of less than \$50,000). Overall, these results indicate an increase in the proportion of Incubatees achieving export revenue.

Figure 4.6

#### INCUBATEES REPORTING ANNUAL EXPORT REVENUE, 2000-01 – 2002-03 (PERCENTAGE)



Source: Incubatee Survey results.

### Future Company Performance

In the survey, Incubatees were asked to provide a forecast of what their company's revenue, employment and exports will be in five years time (2008).

The majority of Incubatees were positive about their company's prospects for future revenues, with 78 per cent of Incubatees who responded to the survey forecasting revenue by 2008 (compared with an actual 61 per cent with revenues in 2002-03). Further, Incubatees were confident of significant revenues being achieved — 26 per cent of Incubatees forecast that their company's annual revenue would be between \$1m and \$5m and a further 22 per cent forecast annual revenues of between \$5m and \$10m.

Incubatees were also positive about their future prospects for export revenue, with 70 per cent forecasting export revenues by 2008 (compared with 24 per cent with actual export revenues in 2002-03). Of these, 35 per cent forecast annual export revenues of between \$1m and \$5m.

Finally, Incubatees were positive about their ability to increase the number of employees in their business, with 76 per cent of Incubatees forecasting employment growth for their company by 2008. Of these, 25 per cent forecast FTE employment levels of between 11 and 20 FTE employees.

### ***Value of Investments and Assets***

In the survey, Incubatees were asked to detail the value of their company's investments and assets at 30 June 2003. Of the Incubatees who responded to the survey, 61 per cent reported some assets or investments. The most common assets were physical assets, such as machinery and equipment, with 63 of Incubatees owning some physical assets. The average value of these assets was relatively low, with the majority being worth less than \$30,000. Only 14 per cent of Incubatees reported owning investments. This result is perhaps to be expected given the early stage of development that the majority of Incubatees are in. Finally, 46 per cent of Incubatees who responded to the survey reported owning 'Other Assets'.

### ***Intellectual Property***

An important indicator of business progress and development is the extent of intellectual property protection undertaken. In the survey, Incubatees were asked whether they had taken any steps to protect their intellectual property. Of the Incubatees who responded to the survey, 68 per cent had taken some steps to protect their intellectual property. As shown in Table 4.1, the most common form of protection taken were patents, followed by copyright claims and trademarks. Some 38 per cent of respondents had lodged at least one patent.

Table 4.1

#### **INTELLECTUAL PROPERTY PROTECTION UNDERTAKEN BY INCUBATEES**

|                                  | Percentage of Incubatees | Number of activities |
|----------------------------------|--------------------------|----------------------|
| Patents                          | 38                       | 94                   |
| Copyright claims                 | 19                       | 553                  |
| Trademarks                       | 19                       | 30                   |
| Circuit layout protection claims | 1                        | 2                    |

Source: Incubatee Survey results.

### ***Incubatee Assessments of Performance***

Useful indicators of Incubatee performance can also come from Incubatees' own assessment of their performance, and the measures which they use in assessing their success. In the survey, Incubatees were asked about the success indicators they used for their company.

As shown in Table 4.2, the top success indicator for Incubatees was sales (31 per cent of Incubatees), followed by revenue (23 per cent) and profit (15 per cent). This result indicates that those indicators used to assess Incubatee performance in this Chapter are very similar to those used by Incubatees themselves to assess their own performance.

Table 4.2

**INCUBATEE SUCCESS INDICATORS**

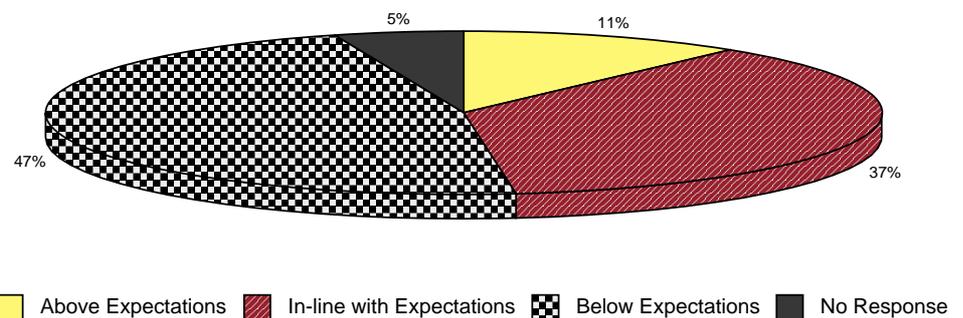
| Indicator |                                |
|-----------|--------------------------------|
| 1         | Sales                          |
| 2         | Revenue                        |
| 3         | Profit                         |
| 4         | Customer satisfaction/feedback |
| 5         | Number of clients              |
| 6         | Product development            |
| 7         | Market acceptance              |
| 8         | Strategic partnerships         |
| 9         | Reaching business milestones   |
| 10        | Return on investment           |

Source: Incubatee Survey results.

Incubatees were also asked about the extent to which their company had progressed in line with their expectations. A range of responses was provided to this question, which have been characterised in three levels of performance, as shown in Figure 4.7.

Figure 4.7

**INCUBATEE ASSESSMENT OF PROGRESS AGAINST EXPECTATIONS (PERCENTAGE)**



Source: Incubatee Survey Results

Almost half of the Incubatees who responded to the survey reported that their company’s progress was below expectations. This result is perhaps to be expected given the difficulties and uncertainties involved with setting up a new company and developing new products and services.

### 4.3 Incubatee Rating of Incubation

Incubatee perception of the benefits of incubation for their business is a key indicator in assessing the effectiveness of an incubation program.

Incubatees were asked to rank the importance of the services that they have been provided during incubation. As shown in Table 4.3, Incubatees rated advice with business planning as the most important service, followed by financial management advice. Interestingly, those services which are more likely to be easily sourced from outside the Incubator, such as legal and accounting services and secretarial services rated low in importance with Incubatees, perhaps indicating that Incubatees see the most important role of their Incubator as providing specialised advice on business development and planning.

Table 4.3

#### INCUBATEE RATING OF IMPORTANCE OF SERVICES

| Rank | Service                             | Score |
|------|-------------------------------------|-------|
| 1    | Advice with business planning       | 2.4   |
| 2    | Financial management advice         | 3.4   |
| 3    | Marketing and sales services        | 3.5   |
| 4    | Networking opportunities            | 3.8   |
| 5    | Mentoring Program                   | 4.0   |
| 6    | Legal or accounting services        | 4.5   |
| 7    | Provision of Incubatee Board member | 4.6   |
| 8    | Secretarial services                | 6.6   |

Source: Incubatee Survey.

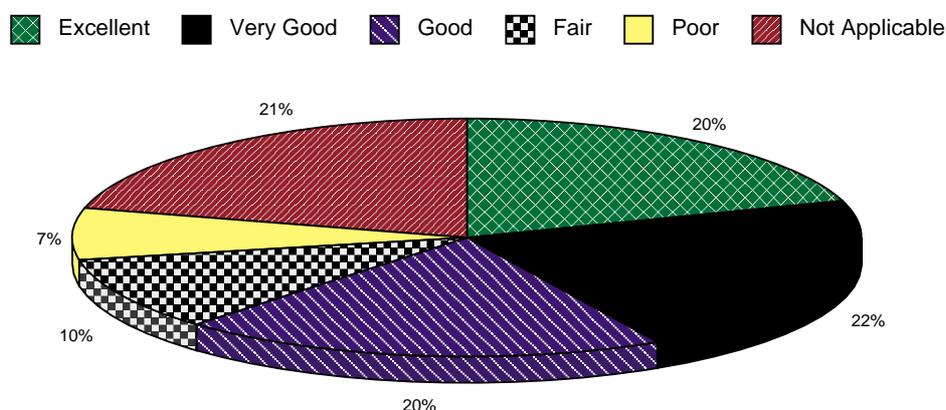
#### *Incubator Ratings*

In the survey, Incubatees were asked to provide an overall rating of their incubation experience. As shown in Figure 4.8, the ratings of overall Incubator performance are relatively positive.

Some 42 per cent of Incubatees rated their Incubator as ‘very good’ or ‘excellent’ and only 7 per cent of Incubatees rated their Incubator as ‘poor’.

Incubatees were also asked to rate their Incubator’s performance in providing a range of services. As shown in Figure 4.9 there is significant variance of ratings across each service. The large number of ‘not applicable’ responses for some services related to those services not being offered by some Incubators (in particular, workshops).

Figure 4.8

**OVERALL INCUBATEE RATING OF INCUBATOR PERFORMANCE (PERCENTAGE)**

Source: Incubatee Survey Results

Overall, the services with the lowest approval rating by Incubatees was the business development training program, with 15 per cent of Incubatees rating it as 'poor', and marketing and sales services, with 12 per cent of Incubatees rating it as 'poor'. Conversely, networking opportunities provided by Incubators was rated relatively highly, with 39 per cent of Incubatees rating it as 'very good' or 'excellent'. The appointment of Directors to the boards of Incubatee companies was also rated highly by Incubatees, with 22 per cent rating it as 'excellent'.

When considering these results in conjunction with Table 4.3, care must be taken to understand the difference between what services Incubatees rate as important, and the how they rated those services that they received. For instance, while 'Provision of Incubatee Board Member' was the second least important service for Incubatees, those Incubatees who received these services gave a high rating to the way in which they were provided.

***Incubatee Suggestions for Additional Services***

In the survey, Incubatees were asked to provide any suggestions for additional services that they felt they would have benefited from during incubation. Overall, only a small number of responses were provided to this question, indicating that Incubatees are relatively satisfied with the range of services provided to them during incubation. Of the 29 responses provided to the question, five used the opportunity to note that they were satisfied with the services with which they had been provided.

Of the suggestions that were provided, the most common was marketing services and sales services, with four Incubatees suggesting each of these. Others included legal services, accounting services and recruitment services. On the whole, the services suggested are those that are provided by some Incubators. One Incubatee suggested that Incubators should provide better verification of external services providers.

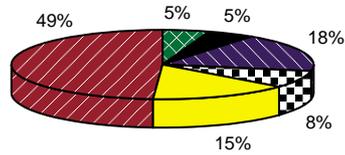
Further views of Incubatees on Incubation are provided in Box 4.1

Figure 4.9

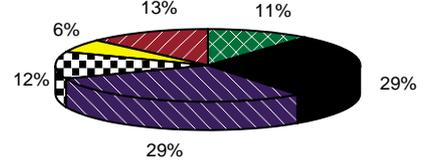
**INCUBATEE RATING OF INCUBATOR PERFORMANCE IN PROVIDING SERVICES (PERCENTAGE)**

Excellent
  Very Good
  Good
  Fair
  Poor
  Not Applicable

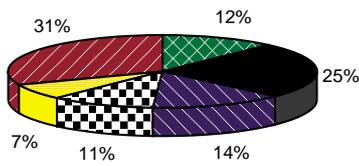
**Business Development Training Program**



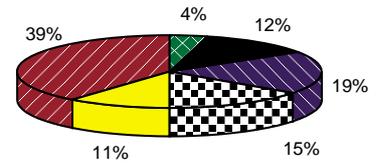
**Advice with Business Planning**



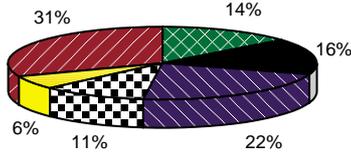
**Financial Management Advice**



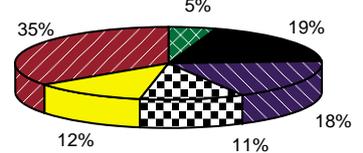
**Legal or Accounting Services**



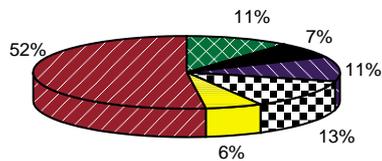
**Mentoring Program**



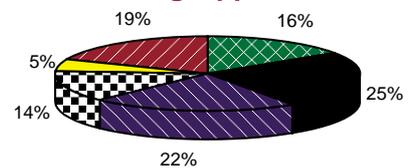
**Marketing and Sales Services**



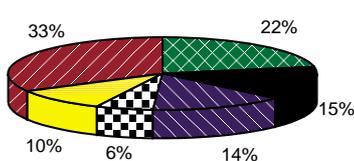
**Secretarial Services**



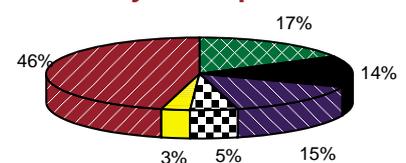
**Networking Opportunities**



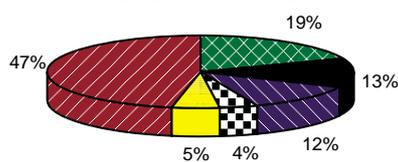
**Provision of Incubatee Board Member**



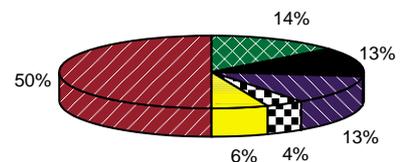
**Physical Space**



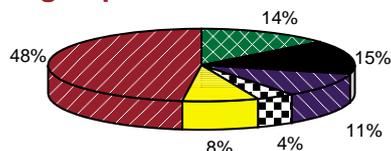
**Office Equipment (copier, fax)**



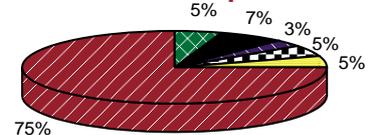
**Server/LAN**



**High Speed Internet Access**



**Workshop**



Source: Incubatee Survey Results

Box 4.1

**INCUBATEE VIEWS ON INCUBATION**

Several Incubatees noted the benefits of the Incubation Programs in providing exposure for their company to commercial investors and venture capitalists, helping to bridge a perceived funding gap at the early stage of business development.

*'Greatest value lies in breaching the "start of investment gap" with potential commercial investors/VC's. The difficulty in sourcing initial capital funding in Australia remains extreme, even for experienced management teams'.*

*'Very good general exposure to commercial experience such as funding, networking and sales and marketing. Networking amongst peers was important to maintain morale'.*

*'Networking/advice/services all very good and difficult to get elsewhere'.*

*'Without them we could not of commercialised (our technology) and it adds credibility and substance to start up'.*

*'The financial assistance and consulting we received from our Incubator was extremely valuable in helping us get through the R&D phase of this new product development. The matching funds that they provided for industry and government sponsored R&D projects set us on a path to commercialisation. This gave us financial strength and industry recognition, as well as leveraging the BITS funds in the commercial arena, its a win-win'.*

*'Best outcome has been helping provide the commercial "weight" to more effectively manage the institutional (Founding) shareholders'.*

One Incubatee noted the overriding importance of funding availability for start-up companies.

*'Without the capital we would not be in business today. Little else has mattered. Technology companies take at least 3-5 years to work out their products, value equation for clients and cash flow positive marketing channels. They need patient capital'.*

One dissatisfied Incubatee came up with an alternative model for the Programs, where Incubatees had more control over the management of funds.

*'Great idea but in the hands of an inexperienced/incompetent incubator little apparent value for money. I suggest only non-profit business models with Incubatees having full control of funds. Incubatees purchase services off incubator if they are performing'.*

Source: Incubatee Survey Responses

#### **4.4 Analysis by Incubator**

While an overall assessment of the experience and performance of Incubatees is useful, given the different services offered and the models of incubation provided by the Incubators, it is important to take this analysis to a more disaggregated level

by Incubator. Further, an overall assessment of Incubatee satisfaction can mask both good and bad performances within individual Incubators.

Analysis by Incubator does provide some challenges with small sample size. For some Incubators, only a small number of responses were received, making any analysis on the basis of these responses dependent on only a small amount of data.

Table 4.4 provides a summary of the performance of Incubatees by Incubator for the financial years 2001-02 and 2002-03, to provide some picture of change over the period of incubation. The majority of Incubatees (71 per cent) responding to the survey had not commenced incubation in 2000-01.

### ***Funding to Incubatees***

As Table 4.4 shows, there is significant variance in the average level of funding provided to Incubatees across Incubators, both as cash and as in-kind services. Of those Incubatees who responded to the survey, InQbator provided the highest average amount of cash funding, and Information City Victoria the lowest. This result for Information City is influenced by the large number of 'limited assistance' Incubatees who responded to the survey. Item3 provided the highest average amount of in-kind services.

### ***Revenue***

Average Incubatee revenue, as reported in the surveys, was highest for the BlueFire Incubator, with average revenue per Incubatee of \$812,800. Original IT had the lowest average revenue in 2002-03, with \$1,666.

For all but one Incubator, average Incubatee revenue increased between 2000-01 and 2002-03. Average Incubatee revenue for Playford fell slightly, a result influenced by one Incubatee whose revenue fell considerably between 2000-01 and 2002-03. Overall, there is a strong trend of increasing revenues for Incubatees across most Incubators.

### ***Employment***

Across all Incubators, average Incubatee employment increased from 2000-01 to 2002-03. Allen and Buckeridge Incubatees had the highest average employment, with 10 FTE employees, a strong increase from 2 FTE in 2000-01.

### ***Profit***

As already noted in the earlier analysis in this chapter, very few Incubatees have achieved profits to date. This is not surprising because at this very early stage, technology companies tend to reinvest their revenues in further product development. This is evident when assessing the disaggregated data by Incubator, with only two Incubators having Incubatees making profits in 2000-01 (BlueFire and Playford). By 2002-03, six of eleven Incubatees had Incubatees achieving profits.

### ***Exports***

As with profits, few Incubatees reported any export revenues in 2000-01. However, by 2002-03, all but one Incubator (Original IT) had Incubatees with export revenue. Allen and Buckeridge had the highest average annual export revenue for Incubatees, closely followed by BlueFire and Playford.

Table 4.4

**RESPONSES TO INCUBATEES & GRADUATES SURVEY – INCUBATEE PERFORMANCE**

|   | A&B<br>NSW | ADI<br>VIC | BlueFire<br>NSW | EiR<br>WA | Epicorp<br>ACT | ICV<br>VIC | InQbator<br>QLD | In-tellinc<br>TAS | ITem3<br>NSW | OIT<br>NT | Playford<br>SA |
|---|------------|------------|-----------------|-----------|----------------|------------|-----------------|-------------------|--------------|-----------|----------------|
| Incubatees receiving significant assistance (1) | 6          | 8          | 7               | 6         | 8              | 9          | 7               | 11                | 5            | 2         | 7              |
| Incubatees receiving limited assistance         | 1          | 2          | 0               | 5         | 2              | 10         | NA              | 1                 | NA           | 1         | 2              |
| Average length of incubation (months)           | 18         | 10         | 20              | 12        | 15             | 10         | 17              | 13                | 25           | 28        | 8              |
| Average cash from Incubator (\$)                | 299,989    | 143,000    | 328,000         | 166,818   | 287,125        | 26,628     | 435,496         | 91,235            | 165,000      | 382,748   | 208,433        |
| Average value of Incubator services (\$)        | 66,667     | 45,000     | 60,714          | 20,455    | 21,875         | 35,714     | 25,000          | 181,250           | 245,000      | 33,333    | 25,000         |
| Average FTE employees in 2002-03                | 10         | 6          | 7               | 2         | 5              | 1          | 3               | 4                 | 4            | 1         | 6              |
| Average FTE employees in 2000-01                | 2          | 3          | 6               | 1         | 2              | 0          | 1               | 0                 | 2            | 1         | 2              |
| Average revenue 2002-03 (\$)                    | 451,769    | 336,121    | 812,800         | 26,836    | 331,125        | 55,214     | 83,012          | 244,148           | 97,400       | 1,666     | 190,650        |
| Average revenue 2000-01 (\$)                    | 74,995     | 140,777    | 484,714         | 6,130     | 141,000        | 0          | 33,631          | 6,083             | 54,686       | 0         | 227,222        |
| Average Profits 2002-03 (\$)                    | 1,400      | 0          | 78,571          | 0         | 6,375          | 8,643      | 0               | 13,333            | 0            | 0         | 886            |
| Average Profits 2000-01 (\$)                    | 0          | 0          | 71,429          | 0         | 0              | 0          | 0               | 0                 | 0            | 0         | 9,778          |
| Exports 2002-03 (\$)                            | 231,429    | 38,300     | 214,486         | 9,091     | 195,625        | 21,429     | 5,579           | 114,667           | 6,000        | 0         | 209,696        |
| Exports 2000-01 (\$)                            | 5,857      | 0          | 0               | 0         | 0              | 0          | 0               | 0                 | 0            | 0         | 168,222        |

Note: 1. Limited assistance is defined as less than \$50,000.

Source: BITS Evaluation Incubatee Survey results.

## Chapter 5

# BITS and Intelligent Island Incubator Performance

### 5.1 Performance — Quantifiable Factors

Table 5.1 presents summary information about the 10 BITS Incubators and the Intelligent Island Incubator in Tasmania, funded through the *Intelligent Island Program*. Except where separately identified, this analysis covers all eleven Incubators. There is one Incubator located in each of Australia's State and Territory capitals, except for Sydney and Melbourne, which have three and two respectively.

The regional Incubators (those in Darwin, Hobart, Adelaide and Perth and Canberra) face a range of challenges that the major city Incubators largely escape, including a lack of supporting structures, difficulties accessing business angels and venture capital, lower quality and quantity of deal flow, and problems associated with small local markets for Incubatee products and large distances from major population centres. Basic Incubator data is summarised in Table 5.1. Incubator inputs and outputs to 30 June 2003 are summarised in Table 5.2. Incubator services and equity arrangements are summarised in Table 5.3.

#### 5.1.1 Incubator Operations

##### *The Incubator Models*

Three key features of the Incubators' business models can be distinguished.

- For-profit or not-for-profit companies.
- Physical Incubators that provide office space to Incubatees and virtual incubators, which do not. Incubators can work in both modes (*mixed*).
- Incubators that provide cash, and receive equity in Incubatees and Incubators that receive equity in return for services provided. Some incubators provide a mix (*blend*) of cash and services.

Most of the Incubators are for-profit. There are also two not-for-profit operations (Playford Capital and Epicorp). Eight Incubators provide physical or physical/virtual incubation, while three of them offer only virtual incubation. Where virtual incubation is offered, it is usually supported by strong communication channels that include person-to-person intensive assistance on a weekly basis and telephone/email channels.

Table 5.1

**INCUBATORS - BASIC DATA TO 30 JUNE 2003**

|   | <b>A&amp;B</b>                 | <b>ADI</b>                    | <b>BlueFire</b>             | <b>EiR</b>                  | <b>Epicorp</b>                         | <b>ICV</b>                         | <b>InQbator</b>             | <b>In-tellinc</b>            | <b>ITem3</b>                 | <b>Original IT</b>           | <b>Playford</b>                   |
|---|--------------------------------|-------------------------------|-----------------------------|-----------------------------|--|------------------------------------|-----------------------------|------------------------------|------------------------------|------------------------------|-----------------------------------|
|   | <b>NSW</b>                     | <b>VIC</b>                    | <b>NSW</b>                  | <b>WA</b>                   | <b>ACT</b>                             | <b>VIC</b>                         | <b>QLD</b>                  | <b>TAS</b>                   | <b>NSW</b>                   | <b>NT</b>                    | <b>SA</b>                         |
| Incubator model (1)                         | For Profit<br>Virtual<br>Blend | For Profit<br>Virtual<br>Cash | For Profit<br>Mixed<br>Cash | For Profit<br>Mixed<br>Cash | Not for<br>Profit<br>Physical<br>Blend | For Profit<br>Physical<br>Services | For Profit<br>Mixed<br>Cash | For Profit<br>Mixed<br>Blend | For Profit<br>Mixed<br>Blend | For Profit<br>Mixed<br>Blend | Not for Profit<br>Virtual<br>Cash |
| Commenced                                   | December-99                    | July-00                       | July-99                     | June-00                     | June-00                                | June-00                            | June-00                     | June-01                      | April-00                     | October-00                   | August-01                         |
| Months of operation                         | 43                             | 36                            | 48                          | 36                          | 37                                     | 37                                 | 37                          | 25                           | 39                           | 33                           | 23                                |
| Total Applicants                            | 752                            | 550                           | 770                         | 225                         | 155                                    | 95 <sup>(4)</sup>                  | 331                         | 118                          | 311                          | 54                           | 297                               |
| Incubatees receiving limited assistance (2) | 6                              | 74                            | 2                           | 7                           | 14                                     | 11                                 | 0                           | 1                            | 0                            | 6                            | 6                                 |
| Incubatees receiving significant assistance | 7                              | 14                            | 11                          | 10                          | 12                                     | 33                                 | 12                          | 11                           | 11                           | 8                            | 11                                |
| Incubatees withdrawn from program           | 7                              | 4                             | 3                           | 0                           | 1                                      | 21                                 | 0                           | 0                            | 1                            | 5                            | 0                                 |
| Total Incubatees                            | 13                             | 88                            | 13                          | 17                          | 26                                     | 44                                 | 12                          | 12                           | 11                           | 14                           | 17                                |
| Total Graduates                             | 5                              | 50                            | 3                           | 6                           | 11                                     | 10                                 | 7                           | 1                            | 3                            | 5                            | 12                                |
| Graduates still trading (3)                 | 5                              | 8                             | 3                           | 6                           | 8                                      | 9                                  | 6                           | 1                            | 3                            | 5                            | 12                                |
| Investment exits                            | 0                              | 0                             | 1                           | 3                           | 1                                      | 0                                  | 0                           | 0                            | 0                            | 0                            | 0                                 |

Note: 1 See text for definitions of terms 'virtual', 'mixed' and 'blend'.

2. Limited assistance is defined as less than \$50,000 in cash and services.

3. Most ADI graduates were individuals who participated in a business training program and did not establish a business.

4. ICV only counted those applications that completed the full application process. Total ICV expressions of interest to 30 June 2003 were 315.

Source: The Allen Consulting Group

Table 5.2

**INCUBATORS – INPUTS AND OUTPUTS TO 30 JUNE 2003**

|   | <b>A&amp;B</b> | <b>ADI</b> | <b>BlueFire</b> | <b>EiR</b> | <b>Epicorp</b> | <b>ICV</b> | <b>InQbator</b> | <b>In-tellinc</b> | <b>ITem3</b> | <b>Original IT</b> | <b>Playford</b> |
|---|----------------|------------|-----------------|------------|----------------|------------|-----------------|-------------------|--------------|--------------------|-----------------|
|   | <b>NSW</b>     | <b>VIC</b> | <b>NSW</b>      | <b>WA</b>  | <b>ACT</b>     | <b>VIC</b> | <b>QLD</b>      | <b>TAS</b>        | <b>NSW</b>   | <b>NT</b>          | <b>SA</b>       |
| Prog. funds allocated                       | \$5.0m         | \$7.0m     | \$6.0m          | \$10.0m    | \$8.0m         | \$8.80m    | \$9.5m          | \$8.0m            | \$7.37m      | \$5.0m             | \$10.0m         |
| Prog. funds received                        | \$4.9m         | \$7.0m     | \$4.26m         | \$7.5m     | \$6.62m        | \$7.26m    | \$7.4m          | \$6.3m            | \$7.3m       | \$4.6m             | \$7.67m         |
| Per cent funds received                     | 98%            | 100%       | 71%             | 75%        | 83%            | 83%        | 78%             | 79%               | 99%          | 92%                | 77%             |
| Other funds received                        | \$1.11m        | \$0.71m    | \$0.56m         | \$0.8m     | \$2.2m         | \$0.91m    | \$1.06m         | \$0.76m           | \$1.15m      | \$2.17m            | \$8.13m (2)     |
| Value of in-kind received                   | \$0.03m        | \$3.2m     | \$0.6m          | \$0.48m    | \$0.9m         | \$3.0m     | \$1.78m         | \$0.43m           | \$0.48m      | \$0.03m            | \$0.03m         |
| Prog. funds provided to Incubatees          | \$1.47m        | \$1.72m    | \$2.55m         | \$3.06m    | \$3.83m        | \$0.92m    | \$4.49m         | \$1.05m           | \$1.4m       | \$3.16m            | \$2.91m         |
| Prog. funds provided on a charge back basis | —              | \$0.6m     | —               | \$0.53m    | \$0.02m        | \$3.35m    | \$0.22m         | \$2.12m           | \$2.76m      | \$0.22m            | —               |
| Angel funds received by Incubatees          | —              | \$2.84m    | \$3.06m         | \$2.15m    | \$5.85m        | \$0.71m    | \$0.61m         | \$1.41m           | \$2.55m      | —                  | \$6.8m          |
| Venture capital received by Incubatees      | \$25.75m       | \$6.25m    | \$0.28m         | \$1.55m    | —              | \$0.3m     | \$3.84m         | —                 | —            | —                  | \$8.0m          |
| Other funds received by Incubatees          | —              | \$0.77m    | \$0.37m         | \$1.34m    | \$4.23m        | \$0.35m    | \$3.31m         | \$1.03m           | \$0.69m      | —                  | —               |
| Total other funds received by Incubatees    | \$25.75m       | \$9.86m    | \$3.71m         | \$5.04m    | \$10.08m       | \$1.36m    | \$7.76m         | \$2.44m           | \$3.24m      | —                  | \$14.8m         |
| Incubator establishment costs               | \$0.70m        | \$0.1m     | \$0.65m         | \$0.07m    | \$0.92m        | \$1.03m    | \$0.22m         | \$0.36m           | \$0.31m      | \$0.12m            | \$0.01m         |
| Compliance costs (3)                        | \$0.2m         | \$0.21m    | \$0.3m          | \$0.41m    | \$0.15m        | \$0.24m    | \$0.15m         | \$0.26m           | \$0.49m      | \$0.01m            | \$0.5m          |
| Average annual cost incubator operations    | \$1.15m        | \$1.0m     | \$0.57m         | \$1.03m    | \$0.63m        | \$0.67m    | \$0.37m         | \$0.69m           | \$1.09m      | \$0.79m            | \$1.76m         |

Note: 1. 'Prog' indicates BITS/Intelligent Island Program.  
2. Playford received significant assistance from the SA Government  
3. Includes application costs and reporting costs to 30 June 2003.

Source: The Allen Consulting Group

Table 5.3

**INCUBATORS – SERVICES AND EQUITY**

|                                   | <b>A&amp;B</b> | <b>ADI</b>              | <b>BlueFire</b>         | <b>EiR</b>              | <b>Epicorp</b>          | <b>ICV</b>              | <b>InQbator</b>         | <b>In-tellinc</b>       | <b>ITem3</b>            | <b>Original IT</b> | <b>Playford</b>         |
|-----------------------------------|----------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|--------------------|-------------------------|
|                                   | <b>NSW</b>     | <b>VIC</b>              | <b>NSW</b>              | <b>WA</b>               | <b>ACT</b>              | <b>VIC</b>              | <b>QLD</b>              | <b>TAS</b>              | <b>NSW</b>              | <b>NT</b>          | <b>SA</b>               |
| Business planning advice          | In-House       | In-House                | In-House/<br>Outsourced | In-House                | In-House                | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House           | In-House/<br>Outsourced |
| Financial Management advice       | In-House       | In-House                | In-House                | In-House                | In-House                | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | Outsourced              | Outsourced         | In-House/<br>Outsourced |
| Legal & accounting                | —              | Outsourced              | Outsourced              | In-House/<br>Outsourced | Outsourced              | Outsourced              | Outsourced              | In-House/<br>Outsourced | Outsourced              | Outsourced         | In-House/<br>Outsourced |
| Mentoring program                 | —              | In-House/<br>Outsourced | Outsourced              | In-House/<br>Outsourced | In-House                | Outsourced              | In-House/<br>Outsourced | In-House                | Outsourced              | In-House           | —                       |
| Marketing & sales                 | In-House       | In-House                | In-House                | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | Outsourced              | In-House/<br>Outsourced | In-House/<br>Outsourced | Outsourced         | In-House/<br>Outsourced |
| Secretarial services              | —              | Outsourced              | In-House                | Outsourced              | In-House                | In-House                | Outsourced              | In-House/<br>Outsourced | In-House                | In-House           | —                       |
| Networking                        | In-House       | In-House                | Outsourced              | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House/<br>Outsourced | In-House           | In-House                |
| Meeting rooms                     | In-House       | In-House                | In-House                | In-House                | In-House                | In-House                | In-House                | In-House                | In-House                | In-House           | In-House                |
| Relationship with investment fund | yes            | no                      | no                      | no                      | yes                     | yes                     | yes                     | yes                     | yes                     | yes                | no                      |
| Incubatee Board member            | —              | In-House                | In-House           | —                       |
| Incubator staff at 30/6/03        | 1              | 1                       | 2                       | 3.5                     | 5                       | 6.8                     | 4.4                     | 5.5                     | 3                       | 2                  | 8                       |
| Average annual incubator staff    | 5.0            | 3.8                     | 3.3                     | 2.7                     | 3.7                     | 7.0                     | 4.0                     | 3.8                     | 5.3                     | 3.0                | 9.5                     |
| Equity in Incubatees - average    | 0-25%<br><5%   | 2-31%<br>15%            | 5-45%<br>15%            | 7-45%<br>29%            | 1-30%<br>17%            | 3-45%<br>15%            | 5-39%<br>20%            | 8-40%<br>25%            | 5-45%<br>28%            | 30-40%<br>38%      | 1-17%<br>7%             |

Source: The Allen Consulting Group

### ***Period of Operation***

The first Incubator commenced operations in July 1999 (BlueFire), and so has been operating for 48 months. Most of the others commenced in 2000, although Playford Capital and In-tellinc opened their doors mid 2001. The average time that the Incubators have operated for is 36 months. Even in normal circumstances, experience elsewhere suggests that these are very short periods for a new incubator to reach sustainability. In the particular circumstances following the 'tech wreck' where opportunities to exit such early stage investments has been extremely limited, the time period elapsed to date is too short for the Incubators to realise their full potential. In addition, in 2002 the R&D Start Program, which supports business R&D, did not accept new applications for a period of about seven months. This problem also slowed the progress of some Incubatees.

### ***Setting-up, Running and Compliance Costs***

The Incubators estimated setting up (or establishment) costs averaged just over \$400,000. Again there was considerable variation between the Incubators. For example, three Incubators reported setting up costs of over \$700,000, while one (Playford Capital) reported setting up costs of only \$12,000.

Running (or operating) costs similarly varied, with an average across the Incubators of just under \$1m per annum. Five Incubators reported annual costs of over \$1m, and one (InQbator) reporting annual costs of only \$366,000.

Compliance costs are typically difficult to calculate and survey respondents have difficulty in providing quality estimates of this indicator, with a tendency to overestimate the true costs. The compliance costs reported by the Incubators from the start of the grant period up to 30 June 2003 averaged \$264,000. As could be expected, the estimates varied markedly, from \$7,000 (Original IT) to more than \$485,000 for Item3 and Playford Capital. A few Incubator managers considered that compliance costs associated with the Programs were excessive for a granting program of its size.

### ***Contributions to Incubators***

Funds committed by the Australian Government to the BITS and Intelligent Island Incubators varied from \$5m to \$10m, with the average amount being \$7.7m. Most of these funds have been paid to the Incubators, with approximately \$15m of the nearly \$85m total allocation yet to be received by them at 30 June 2003.

Some \$20m of other funding from sources other than the BITS and Intelligent Island Programs was received by the Incubators, at an average of \$1.6m per Incubator. Most of this funding came from shareholders or guarantors.

### ***In-kind contributions from the business community***

The Incubators were successful in attracting in kind contributions from the business community, reporting totals valued at around \$10.5m, or just over \$950,000 per Incubator. However there was considerable variation between the Incubators in their ability to obtain contributions from the business community. Three of the Incubators reported in-kind contributions of around \$25,000, whereas two of the Incubators reported in-kind contributions of over \$3m.

In some cases, business in-kind contributions were provided to Incubatees through the Incubators. The percentage that went to Incubatees varied from zero (four Incubators) to more than 70 per cent (two incubators).

### ***Incubator Partners and Sponsors***

The Incubators have been very successful in attracting partner or sponsor organisations to join them, with most welcoming major organisations on board in consortium arrangements. Over 30 separate organisations have signed up to assist the Incubators, covering the following broad areas.

- Venture capitalists.
- Major accounting and legal firms.
- ICT companies covering both software development and hardware manufacturing.
- Multimedia companies.
- Research firms.
- Government laboratories and Universities.
- Telecommunications companies.

### ***Relationship with Investment Funds***

Their Grant Deeds required the Incubators to develop a close relationship with an investment fund. In practice, seven out of the 11 Incubators did so, with the remainder either preferring (or being forced to) seek funds on a case-by-case basis. Interestingly, it appears that for the majority of Incubators that reported that they had developed such a relationship, few of them reported that the relationship had led to investment in their Incubatees by that investment fund. This is almost certainly a function of the weak venture capital market in Australia, especially since 2001. In addition, venture capitalists advised that they considered many of the investment opportunities provided by BITS and Intelligent Island Incubators to be too early and too small.

### ***Incubation Facilities***

Physical incubation facilities were provided by eight of the Incubators. Most provided office services including receptionist and typing services, and equipment such as photocopiers, faxes, server and LAN facilities, plus high speed Internet access.

### ***Equity and Service Provision***

The average amount of equity taken in Incubatees by the Incubators was reported as 21 per cent and there was not much variation between Incubators in this indicator.

All of the Incubators take equity in their Incubatees in return for cash and other assistance provided. In limited circumstances, some Incubators provide non-Australian Government funds (or funded services) to Incubatees and may do so through non-equity arrangements.

Incubatees purchased services from their Incubator, from one of their Incubator's recommended service providers or from elsewhere. Some of the Incubators (such as InQbator and BlueFire) were far more willing than others to allow their Incubatees to choose from where they purchased their professional services. In general, those Incubatees who were able to choose for themselves seemed to be far happier with the arrangement, than those who were not allowed to make this choice. In Incubators where the proportion of investment given as cash to Incubatees was low, the survey respondents often reported that they would rather have had more cash than services.

### ***Performance Against Milestones***

Milestones were negotiated individually for all of the BITS incubators after their business proposals were selected on merit in a competitive selection process held in 1999-2000. The Intelligent Island Incubator milestones were developed in a similar way.

These milestones formed part of the schedule to the Grant Deeds and reflected the different approaches taken by the Incubators. They included timeline requirements to establish the infrastructure for Incubator operations, the appointment of qualified management personnel, achievement of progressive targets for processing applications, acceptance of new companies as Incubatees (with or without direct investment), graduation of Incubatee companies and submission of budget and progress reports on time.

DCITA recognised that market conditions in the ICT industry had dramatically changed after the "tech wreck" of 2000 and negotiations were held with most Incubators, leading to lower milestone targets that better reflected prevailing market conditions.

Overall, Incubators have performed creditably against all milestone targets in the first few years of the BITS and Intelligent Island Incubator Programs and reporting has generally been punctual. While milestones regarding the establishment of the Incubators were achieved within timeframe requirements, there were occasions when milestones for accepting new Incubatee companies or processing applications could not be achieved or were achieved later than originally expected.

The continued flat state of the ICT sector led to discussions with the Incubators about the cap of \$450,000 on investment in individual companies. It was agreed that some flexibility would be permitted to allow Incubators to provide up to \$600,000 to a limited number of Incubatees, and a number of Incubators have availed themselves of this facility.

### ***Applicants seeking Incubation***

The number of applicants screened by the Incubators varied greatly — an average of 332 applicants per Incubator over the period to 30 June 2004. Two Incubators screened over 750 applicants each, while one Incubator screened just 54. Some 3,658 applicants have sought assistance from the Incubators since funding under the BITS and Intelligent Island Programs commenced (1999 and 2001 respectively). This enormous demand greatly exceeded the assistance available. In this regard, a number of the Incubator managers commented that the screening process was a very costly aspect of the business that reduced the resources available to assist Incubatees.

The number of proposals reviewed each year by the Incubators has generally declined over the period since 1999. There are two possible explanations for this decline. The first is that there was a high initial demand because of a previous lack of such facilities. The second reason, given by the Incubator managers, is that over time, improved judgement by the Investment managers in the initial screening of applicants was driven by a realisation that processing applications is a costly exercise and a concern not to abandon Incubatees 'mid-stream' with the approaching end of the grant period.

Up to 30 June 2003, the Incubators report that 127 companies received assistance valued at less than \$50,000 and 140 companies received assistance valued at more \$50,000. One Incubator (ADI) can be classified as a high throughput Incubator in that most of the assistance which it has provided to individual Incubatees has been valued at less than \$50,000, in the form of a structured business development training program.

Some other Incubators provide preliminary assistance to prospective Incubatees principally as part of a screening mechanism that assists with the due diligence process. For others still, small initial investments are deemed useful because the judgement is made that larger cash injections are not appropriate, particularly where proof of concept has yet to be established. On average, the Incubators have provided intensive assistance to 13 Incubatees and limited assistance to a further 13 Incubatees.

Some of the Incubators service many firms, whereas others concentrate their efforts on only a few companies. Incubator throughput is not an especially meaningful indicator of success for the BITS or Intelligent Island Programs at this time. The throughput rates vary significantly, reflecting factors such as the different Incubator business models, demand for incubation, resources available to the Incubators and the varying lengths of time that the Incubators have been in operation. Further, there is no relationship between throughput and Incubatee success, which is more appropriately measured by other indicators.

The Incubators use different definitions of the term 'graduation'. Graduation can be defined by one or more of the following.

- End of incubation agreement.
- Significant sales/revenue.
- Follow-on investment.
- Sustainable business.
- Trade sale or listing.

It is too early to accurately gauge failure rates for Incubatees, as measured by the number of graduates that are no longer trading. However, the Incubators reported that 39 out of 49 Graduates (around 80 per cent) that received less than \$50,000 in assistance are still trading.<sup>31</sup>

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<sup>31</sup> The proportion in respect of Graduates that received less than \$50,000 and are still trading is 35 per cent, although this number is not firm because Incubators that provide services to this group have had difficulty in maintaining contact with their Graduates.

The number of Incubatees that withdrew from incubation was fairly low, which is probably a reflection of the rigorous selection processes on the part of the Incubators and the quality of Incubatees.

### **5.1.2 Assistance Provided to Incubatees**

#### ***Program Funds Invested in Incubatees***

On average, most Incubators invested less than half of their grants in the form of cash provided to Incubatees. There was considerable variation between individual Incubators. For example, InQbator stood out in providing around 90 per cent of its BITS grant to its Incubatees in cash. BlueFire, Epicorp and Original IT all provided more than 50 per cent of their BITS grants to their Incubatees in cash.

The other seven Incubators chose to provide most of their Government grants to Incubatees in the form of services, with less than 50 per cent of their grant being provided in the form of cash. ICV and In-tellinc provided 13 and 17 per cent respectively in cash. While In-tellinc's Incubatees reported (in the survey) that they considered that the in-kind services provided represented value for money, only around half of ICV's Incubatee respondents did. However, this view of ICV's services may not be a true representative of its 'average' Incubatee because of a likely response bias – that is, unhappy respondents might have been in the minority, but more motivated to respond to the survey than their happier counterparts.

#### ***Help in seeking other government assistance***

Many of the Incubatees reported that they helped their Incubatees in seeking other government assistance, such as through R&D Start, COMET and Austrade. While some are more pro-active than others in playing this role, most of them report success in facilitating the raising of additional funds by their Incubatees through other government channels. The Incubators reported that they had been able to assist in the raising of some \$9.3m from Australian Government sources and approximately \$630,000 from State and Territory Government sources.

Typically, ADI has regularly invited COMET and Austrade operational managers to speak at events for its Incubatees to inform them of the process for applying for assistance. Incubator managers find preparing grant applications time consuming and best outsourced to specialists. In some circumstances ADI has helped write applications. In some cases, Incubatees themselves have taken the initiative to apply for assistance.

#### ***Assistance with Capital Raising***

In addition to providing help in accessing government funds, the Incubators assisted their Incubatees to raise funding from other sources — indeed this was a requirement under the Grant Deeds for all the Incubators. The Incubators estimate that they played a facilitating role in the raising of some \$74m in additional investment, most of which came from venture capitalists (\$46m) and business angels (\$26m).

### ***Assistance with Business Planning***

All the Incubators assisted their Incubatees (and often applicants for incubation) with business planning. Most of the Incubators provided a business development training program as a service to their Incubatees. In addition, most provided ongoing informal or occasional assistance with business training either in-house or outsourced. All the Incubators assisted Incubatees with their business plans. In some cases this required the complete development of the business plan while in others it involved improving an existing plan.

### ***Assistance with Business Development***

One of the most important roles played by all incubators is helping Incubatees to grow their businesses. Sales are an important element of this business development. Finding major companies that will agree to be a test site for the development and demonstration of a new product often requires access to chief executives in target corporations. These customers help to complete the development of the product and become important references for further sales. In this regard, the Incubators have played an important door-opening role.

Another business development activity to which the Incubators have made an important contribution is helping Incubatees to form technology partnerships and other business alliances with global corporates such as Sun and IBM. These alliances can result in Incubatees receiving valuable technical information as well as helping with market access.

Incubatees also value assistance from their Incubators in finding experienced Directors to serve on their Boards. Finding Directors who are willing to serve on the Boards of start-up companies is not easy. Incubator managers have used their connections to find these Directors, who often feel more comfortable in this role because of the active involvement of the Incubator.

Some Incubatees have been allocated mentors by their Incubator. Mentors have received little or no remuneration. The performance of these mentors received mixed reviews from the Incubatees and Graduates that were interviewed.

### ***Other Services Provided to Incubatees***

The Incubators provide a wide range of other services to their Incubatees, most of which are provided in-house, although legal or accounting services and a mentoring program were generally outsourced.

The Incubator and Incubatee questionnaires asked respondents to not only indicate which Incubatee services were provided by Incubators, but also to rank the relative importance of these services (relative to each other) in terms of how they contribute to a successful incubation experience for Incubatees (see Table 5.4).

It is notable that while the Incubators and Incubatees agreed that advice with business planning as being most important (ranking = 1) and secretarial services as being the least important (ranking = 8) they differed on the importance of most other services. An interesting difference was that Incubators ranked the provision of an Incubatee Board member as being the third most important service, whereas Incubatees ranked it as being the seventh most important service.

Table 5.4

**INCUBATOR AND INCUBATEE RANKINGS OF THE IMPORTANCE OF SERVICES PROVIDED TO INCUBATEES**

|                                     | <b>Incubatees</b>         | <b>Incubators</b>         |
|-------------------------------------|---------------------------|---------------------------|
|                                     | <b>Importance Ranking</b> | <b>Importance Ranking</b> |
| Advice with business planning       | 1                         | 1                         |
| Financial management advice         | 2                         | 4                         |
| Marketing and sales services        | 3                         | 2                         |
| Networking opportunities            | 4                         | 5                         |
| Mentoring program                   | 5                         | 6                         |
| Legal or accounting services        | 6                         | 7                         |
| Provision of Incubatee board member | 7                         | 3                         |
| Secretarial services                | 8                         | 8                         |

Source: Allen Consulting Group Survey for Incubatees and Incubators – Survey results.

## 5.2 Performance — Quality Factors

This evaluation has discussed and analysed a number of quantitative measures of Incubator performance. However, qualitative factors also need to be considered.

Table 2.1 in Chapter 2 lists a set of quality factors applicable to the Incubators. Assessing Incubator performance against this list is complicated by the very different business models and operating environments of the Incubators. For example, the Darwin Incubator does not have the same working environment as a Sydney Incubator. Not all of the items listed in Table 2.1 apply to all the Incubators. For instance, virtual incubators are not assessed on the basis of Incubator facilities.

Assessment of the Incubators was based on interviews with Incubatees, Graduates, Incubator Managers and some Incubator Board members, venture capitalists and other financiers and State and Commonwealth Government officials. Input was also obtained from surveys of the Incubators, their Incubatees and Graduates.

The ratings in Table 5.5 are necessarily subjective, and represent a composite assessment drawing as appropriate from the components listed in Table 2.1. They also represent an assessment of quality factors over the previous three years, rather than an assessment of these factors at 30 June 2003.

Table 5.5

**INCUBATORS – QUALITATIVE FACTORS**

| Overall Quality Rating | Incubators   |
|------------------------|--|
| Excellent              | InQbator, Playford, Epicorp                          |
| Very Good              | BlueFire, EiR, In-tellinc, Information City Victoria |
| Good                   | Allen & Buckeridge, ADI, Item3                       |
| Fair                   | Original IT  |

Note: This table has been developed using a balanced scorecard approach  
Source: The Allen Consulting Group

***Governance and Management***

The makeup of the Incubators' Boards varies widely. Some appear to have a good balance of skills including legal and financial expertise. Others are more limited, or have only recently achieved an optimal balance of Board member skills and experience. Forming a judgement on incubator Boards, however, is not easy. For example in one case the Board is small but the Directors have a strong and direct interest in the success of the Incubator. Some have clearly delineated roles for the Board and the management. In these instances, management commented that its judgements on investments were sometimes over ruled by the investment committee of the Board.

The experience of Incubator Managers also varied. Few had any previous experience in working in a business incubator, while some had business experience including involvement in ICT start-ups. While this is useful in terms of understanding the clients' needs, being able to manage and direct a stable of ICT start ups requires a different mix of business skills and experience.

Most Incubator Boards appear to work together well and have a clear understanding of the Incubator's goals. Some Boards include independent directors and/or an independent Chair.

***Enterprise Development Assistance***

All the Incubators perform rigorous diagnostics on applicants. It has been important to select the best prospects for incubation given the Incubators' limited resources. However the costs involved in this assessment have been significant. Over the period of the funding, some of the Incubators have streamlined their assessment processes to reduce these costs and most comment that they have become more efficient in vetting new investment proposals.

Assistance measures provided by the Incubators vary in terms of intensity and, based on the survey responses of the Incubatees, also vary in quality and usefulness. While some Incubatees were very satisfied with the services provided by their Incubator, others were not confident that the services they received represented value for money. This is reflected in Figure 4.1 in Chapter 4. In this regard, it should be recognised that the response rates for some of the Incubators were low and therefore probably do not represent the views of the 'average' Incubatee.

Some, but not all, of the Incubators provide mentors (see Table 5.3). Satisfaction with mentors probably depends on the individuals involved and whether they were jointly chosen by the Incubator and Incubatee or whether the appointment was the decision of the Incubator.

Graduation has been discussed earlier in this Chapter and appears to be less important than some of the other factors.

Most of the Incubators have systems in place to track the assistance that they provide even if in some cases these systems are very simple.

### ***Marketing Strategy***

None of the Incubators have yet reached a steady state, where the flow of Incubatees matches the outflow of Graduates. This is because of the difficulties they have faced in achieving exits from their investments. However as might be expected, some of the Incubators appear to have managed their environments more effectively and therefore look more viable than others. In particular, some of them have been active in developing other Incubator revenue opportunities as a way to shore up their survival. That said, at the present time, and without further Australian Government funding, the future of many of the Incubators does not look secure.

Most of the Incubators have shown some targeting of prospective Incubatees, particularly as time has passed, although this is less evident in those Incubators located in some of the regional areas.

The Incubator managers are all able to clearly articulate the benefits they have provided to their Incubatees, although these benefits are not always as clearly recognised by their Incubatees. Managing the expectations of Incubatees has not been an easy task. Early expectations about raising venture capital were not able to be realised in a number of cases although this has generally not been because of a lack of effort by the Incubator.

In general, but not in all cases, business assistance was tailored to the needs of individual Incubatees.

### ***The Incubator Facility***

In most cases those Incubators that provide physical facilities have a building that is attractive to the Incubatee market, which they are seeking to service. They have common space, although the quality of this space varies. All of the Incubators are well equipped with local area networks and high-speed Internet access. Most have flexibility in the utilisation of their space to meet Incubatees' changing needs.

### ***Financial Model***

The Incubators' business models tend to reflect world trends at the time that they were established. In this period, for-profit virtual incubators were popular. Subsequent overseas experience suggests that many recently established ICT incubators with these characteristics have struggled to survive.

Apart from the present difficulties facing those Incubators that have used nearly all their Government funding, there is no evidence to suggest that the Incubators have been burdened by facility costs. Rents charged to Incubator tenants are at or near market rates in most cases. Most Incubators have been able to secure their premises on peppercorn rental terms from local governments or Universities.

Managing risks has been difficult for the Incubators. The major risk has been that of not being able to obtain early returns on their investments — a risk largely outside the control of the Incubators in the short period of their operation.

## Chapter 6

# Conclusions and Findings on the Incubators

Most of the Incubators examined in this evaluation have demonstrated that they are highly effective in assisting start-up and early stage ICT companies to establish their businesses and develop markets for their products.

Many of the businesses that have benefited from incubation and are now ‘going concerns’ with good prospects, employing staff and generating profits. There is evidence that many of these businesses would have struggled without assistance from the Incubators. The support provided by Incubators, with a mix of capital and business support, places these Programs in a specialised position to support start-ups in a way that other Programs do not.

Australia has a relatively small market for new ICT products and services, along with limited support measures for assisting ICT start-ups. This makes it very difficult for ICT start-ups to get any traction in the market. The Incubators have made an important contribution in assisting these firms to overcome these limitations.

The previous Chapter analyses the performance of the individual Incubators. This gives rise to some issues that require further discussion.

### 6.1 Key Design Factors Impacting on Incubator Success<sup>32</sup>

Previous attempts to link design characteristics with incubator success have not been able to find significant correlations. Most previous studies have not been able to demonstrate that particular design factors are determinants of incubator success. One recent study<sup>33</sup> suggests that there is evidence to support the view that physical incubators have some advantages over other forms of support for business development (eg venture capital providers and virtual incubators).

Another recent report by the NBIA<sup>34</sup> sought to define the outcomes achieved by different incubator practices, with a view to identifying best practice. The study team identified 17 ‘best-in-class’ incubators on the basis of their performance in achieving revenue and employment growth in their incubatees. The majority of these incubators were found to have a strong working relationship with a research-intensive university, institute or laboratory, or were located in a metropolitan area that had a high concentration of technology-based companies and service providers providing support.

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<sup>32</sup> This section draws on comments provided by Greg Horowitz and his colleagues at UCSD. Note that CONNECT incubator operates on a self-supporting basis without physical incubation space (see Appendix A for more details).

<sup>33</sup> Johnsrud, C S, Theis, R P and Bezerra, M, 2003, “Business Incubation: Emerging Trends for Profitability and Economic Development in the US, Central Asia and the Middle East”, a report prepared for the US Department of Commerce.

<sup>34</sup> Tornatzky, L, Sherman, H, Adkins, D, 2002, “A National Benchmarking Analysis of Technology Business Incubator performances and Practices”, a report by NBIA to the Technology Administration, US Department of Commerce.

This NBIA study shows that about 48 per cent of technology incubators were focussed on ICT and 24 per cent on biotechnology and biomedical applications. Interestingly, The biotechnology/biomedical incubatees were found to have raised more money, obtained more research support and held more patents than other incubatees.

More importantly, while the NBIA study showed no strong correlations between the business assistance practices of the incubators and outcomes such as incubatee sales and revenue growth, it did show positive correlations between these practices and equity investment, patents, research grants, copyright and licensed intellectual property. The skills of the individual incubator managers provide a possible predictor of performance.

#### *Physical Incubation versus Virtual Incubation*

This depends on the particular incubatee company and the incubator in question. Many members of NBIA are physical incubators that provide space at a publicly subsidised cost. Physical incubation leads to a lower number of companies assisted in any given time period but the form of the assistance can be more in-depth than in a virtual incubator.

Best practice for a physical incubator is to increase the rents charged as the company grows up and to have a clear strategy in place at the start of incubation for the firm to graduate from the incubator thus allowing for natural turnover in the incubator space.

Best practice in a virtual incubator is to maximize the number of networking events for member companies and entrepreneurs to network with local venture capitalists, angel investors and high tech business service providers such as intellectual property lawyers. Furthermore, a virtual incubator should maximize the opportunities to tap local business leaders as volunteers in activities that can serve dual purposes: networking with their peers and business development opportunities for the firms these business leaders represent.

#### *For-profit versus not-for-profit Incubators*

This evaluation has found no evidence to suggest that, in the longer term, for profit incubators should be any more (or less) successful than not-for-profit incubators. In order to attract capital, for-profit incubators must either demonstrate that they can provide returns on investment or attract sponsors with other motivations (such as future investment and business opportunities) to provide cash.

#### *Incubation Cash versus Services*

Should the Incubators use funds for cash injections or to pay for a provision of a range of services? This depends on the company being assisted. Incubatees showed a preference for their Board (on which the Incubator is usually represented) to decide on which services will be purchased and from which providers. However the Incubators may wish to take the position that their investment is conditional on the purchase of certain services. In these circumstances, the Incubatee needs to be convinced that the services offered by the Incubator offer value for money and are necessary for the company's growth.

The consensus seems to be that for assistance to be effective, the assistance must be specific to that company's needs at the time of incubation. Tailoring services and subsidies to each company's needs also makes it hard to perform meaningful evaluations. So striking a balance between cash and services is key.

### *The Incubators' Business Models*

The BITS and Intelligent Island Incubators adopted business models that reflect the nature of the ICT sector at the time they commenced operated. The combination of virtual, for-profit and equity-in-return-for-services models adopted by a number of the Incubators was untested in Australia, especially in periods of 'normal' business activity. In this regard, the BITS and Intelligent Island Incubators are somewhat experimental in character.

One feature of the Incubators' business models was the objective to achieve self-sufficiency by the end of a four-year period of Australian Government support. This objective, while commendable, was optimistic, even in the circumstances of the time.

The BITS and Intelligent Island Incubators are focussed on the ICT sector and were conceived at a time when that sector was enjoying unparalleled success. Share prices were growing rapidly and investment capital was readily available for new businesses with good prospects. Initial public offerings of shares were an almost daily event. In Australia, government initiatives had facilitated increased availability of venture capital that had previously been very scarce. However, the collapse in ICT share prices that occurred in April 2000 meant that self-sufficiency in a four-year period could not be achieved.

The Incubators have had to operate in a much more difficult market — more difficult than could have been anticipated. During 2000, the ICT market dropped to levels of activity well below that of the previous decade and there was a significant decline in ICT share prices (the 'tech wreck'). Venture capital, especially early-stage venture capital, almost disappeared. In addition many business angels who had lost money on ICT ventures were reluctant to make new investments in this sector.

After the 'tech wreck', the instability of the capital markets means that there is little or no exit strategy available for an Incubator's investments, hence there is no way to recoup cash to generate working capital for sustaining day-to-day incubator operations. In the current climate it is not realistic to expect the BITS and Intelligent Island Incubators to sustain long-term operations by realising profits from equity investments in their Incubatee companies<sup>35</sup> for the reasons discussed below.

One of the consequences of the Incubators taking equity in their Incubatees is that it turns the Incubators into quasi "public venture capital firms" or "investment holding companies." This leads to further complexity. Private venture capitalists in the USA make investment decisions based on a 'ten per cent' rule of thumb:

"in a portfolio of 10 investments, seven will lose money, two will be profitable in seven years but not at high rates of return, and one will perform at or even well above the 40 percent compound return"

Lee, C-M, Miller, W F, Hancock, M G, and Rowen, H S, 2002, "The Silicon Edge: A Habitat for Innovation and Entrepreneurship", Stanford University Press, p. 209.

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<sup>35</sup> Schnitzler, P, 2001, "For-profit incubators fall far from favor. Start-ups face fortunes outside the womb", Indianapolis Business Journal, November 26, 2001;  
DiCarlo, L, 2001, "Incubators On Life Support", Forbes.com, January 18, 2001;  
see also Johnsrud *et al*, *op cit*.

The few investments with high returns have to carry the overall return on investment for all the investments that fail, over a (typically) ten-year period for the venture fund. Private venture capitalists do not have to maximise the number of companies that they incubate, whereas publicly funded incubators feel some pressure to do so.

Private venture capitalists are also paid a management fee and have operating cash flows built into their relationships with their sponsors. They do not have to worry about interim operating cash flows before exiting an investment, as do the publicly funded BITS and Intelligent Island Incubators.

Because the incubatee companies are not quite mature enough for venture capital funding, the risks of firm failure are inherently much higher than the private venture capital rules of thumb quoted above. This makes it difficult for BITS and Intelligent Island Incubators to support future activities solely from investment exits, because these may yield a lower rate of return than those expected by venture capitalists (ie. less than one winner out of ten investments).

In the period following the ‘tech wreck’, the Incubators have had to adapt to these changed circumstances. The extent to which the Incubators acted early to address the consequences of the change in the market is one factor influencing their ability to survive beyond the end of the funding period. The Incubators need to consider further changes towards more sustainable business models.

*Finding 1: The business models adopted by the BITS and Intelligent Island Incubators largely reflected the business conditions at the start of these Programs. The ‘tech wreck’ has had major consequences for the ability of the Incubators to raise capital and to realise returns on some of their investments. The Incubators have had to adjust to these new circumstances and further changes may be necessary.*

#### *The Cap on Incubator Investment*

The BITS Program set a normal limit of \$A450,000 and, in special circumstances \$A600,000 on investments in Incubatees. In terms of limiting the total level of investment (equity, services etc) in a particular Incubatee, any cap should be based on maximizing the number of companies assisted based on the total amount of capital assistance that is available, if that is one of the ‘public good’ missions of the Incubator.

At present there appears to be a significant gap between the total funding that can be obtained from the Incubators and business angels on one hand, and the minimum level of investment that Australian venture capital investors are willing to consider (about \$3m). This investment gap threatens to limit the potential of Incubatees to reach a point where they can attract venture capital. Some Incubatees are currently trying to ‘grow organically’ (ie. fund their own growth from revenue) to bridge this gap. While this may work for some Incubatees, in other cases the market opportunity will be seized by competitors. In these circumstances the present investment cap needs to be reconsidered.

*Finding 2: There is a case for raising the present cap on investment in individual Incubatees.*

### *Linkage with a Venture Capital Investor*

One of the original requirements of the BITS Program was that Incubators demonstrate that they had established a link with a venture capital investor. Most of the Incubators have established such a relationship. However in most cases little or no investment in Incubatees has resulted. There appear to be several reasons for this. Venture capital investors have informed the review team that the deals offered were too small and too early. Most Australian venture capital investors sharply reduced their rate of new investments during the period that the BITS and Intelligent Island Incubators have been operating. In addition, some venture capital investors see the Incubators as competitors in the venture capital market.

The evaluation project team considers that the original requirement for a relationship with a venture capital investor is appropriate and that the Incubators should continue to seek and build working relationships with venture capital providers. There is no need for Incubators to limit this relationship to a single provider.

### *Availability of Venture Capital*

The general perception on the state of seed stage investment in the USA, three years on from the 'tech wreck', is that funds are again becoming available in this area. Venture capital funding is not expected to return to the exuberant heights of 2000 but is reported to have stabilized in the past year<sup>36</sup>. In CONNECT's experience, venture capital is available to companies with solid business plans. From CONNECT's experience, the deals in the current pipeline are of much higher quality than those that were struck just before the 'tech wreck'. In addition, company valuations are also much lower than those immediately prior to the 'tech wreck'.

The availability of early stage venture capital is critical to the success of the BITS and Intelligent Island Incubators. The Pilot Evaluation discussed this problem (Section 4.2) and noted the passage of new Australian Government legislation to allow venture capital funds structured as limited partnerships. Venture capitalists supported by IIF Program have already made some investments in Incubatees and have indicated that, if further funds are allocated through this Program, more investments are likely.

*Finding 3: The new limited partnership venture capital funds are unlikely to have any impact before the second half of 2004 and even after that time, the extent to which they might meet the needs of the Incubators is uncertain. In the meantime the Government should provide further funding for the IIF Program and tighten the requirements for early stage investment by the IIFs.*

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<sup>36</sup> PriceWaterhouseCoopers Money Tree Report, available at [http://www.pwcmoneytree.com/moneytree/pdfs/MT\\_Report\\_Q2\\_03\\_Final.pdf](http://www.pwcmoneytree.com/moneytree/pdfs/MT_Report_Q2_03_Final.pdf)

## 6.2 Incubator Performance Measures

The BITS and Intelligent Island Incubators have adopted different investment strategies which make comparisons between the Incubators a challenging task. One of the more significant differences is the nature of the companies in which they have invested. For example, one Incubator has aimed to select only those ventures that have the prospect of becoming international-scale companies with potential turnover in excess of \$100m per annum. At the other end of the spectrum, another Incubator has accepted companies whose prospects are more modest, but are nevertheless capable of growing to be at the very least, self-sustaining, profitable SMEs that create employment, and generate domestic and export revenues. Other Incubators are positioned somewhere between these two extremes.

In relation to measures of success, each of the Incubators was established with individually tailored performance indicators, reflecting the different models that they operate. That said, it is possible to identify a number of measures of success that can be used to evaluate the performance of the Incubators.

At the Program level:

- *Leverage of Program funds* — the extent to which the Incubators have been able to use Program funds provided by the Australian Government to leverage resources (cash and in-kind) for their Incubator and Incubatees from other sources.
- *Total in-kind contributions leveraged* — this is an overall measure of the ability of Incubators to obtain non-cash contributions both for themselves and for their Incubatees. It reflects the Incubators' ability to convince others to contribute advice, equipment, or premises to the Incubator and its Incubatees.
- *The extent to which Incubators have achieved self-sustaining operations* — the BITS and Intelligent Island Incubator Programs aim to create high growth, high value companies, and are based on Incubators being substantially self-sustaining businesses. This includes being able to achieve investment exits (where a return on a capital investment is achieved and usually involves the sale of shares in a graduate or Incubatee) and could also include diversification by Incubators of their sources of funding or revenue.

In relation to the support which individual Incubators have been able to obtain for their Incubatees:

- *Support for Incubatees* — the value of support from all sources that the Incubators have been able to provide to their Incubatees. The extent to which government and other resources reach the Incubatees is a measure of both the efficiency and the effectiveness of the Incubators.
- *Incubatee achievements* — of the various Incubatee performance measures discussed in earlier chapters of this report, the extent to which Incubatees have increased *revenue* is arguably the most relevant performance indicator for the BITS and Intelligent Island Incubators at this stage in their development. Increases in *employment* are problematic given the tendency of start-up ICT companies to contract out requirements as a means of keeping payroll costs down.

- *Incubatee capital leveraged* — the amount of capital leveraged by Incubatees from their BITS investments, with the assistance of their Incubators, is a fundamental measure of success. Failure to leverage outside capital, usually a combination of mostly private and some public funds, makes it impossible for Incubators to help create high growth, high value companies.
- *Incubatee access to business angels* — this is also linked to capital investment. Assistance in finding business angels is an important role of BITS and Intelligent Island Incubators. Business angels help to bridge the gap between funding provided by the Incubator and founders, and venture capital providers. Once the Incubators have established a track record for providing good investment opportunities, they can find business angels more easily for other Incubatees.
- *Incubatee/graduate sustainability* — the extent to which Incubatees and graduates remain viable after receiving intensive assistance is also an important measure of success. While profits would be preferred as a measure of success, it should be recognised that even though many Incubatees are generating revenues, at this stage most are still re-investing revenues back into their businesses. Measures of sustainability include revenue growth and the creation of full time employment. They also include whether or not graduates from the Programs are still trading – normally measured three years after graduation.
- *Satisfaction of Incubatees* — satisfaction of Incubatees with the full package of assistance provided by Incubators is important. Notwithstanding the occasional differences of opinion that characterise most business relationships, Incubatees satisfaction with the type and quality of assistance provided is pivotal to the ultimate success of the Incubatee companies. Success in relation to this factor can be measured by comments received in interviews with Incubatees and the Incubatee questionnaire.

*Finding 4: The BITS and Intelligent Island Incubators have adopted a variety of investment strategies. While some have concentrated their efforts on a small number of very highly prospective ICT start-ups, others have invested in companies whose prospects are more modest, but are nevertheless capable of growing to be self-sustaining, profitable businesses that create employment, and generate domestic and export revenues.*

### **6.3 Quantitative Assessment of Incubator Performance**

Comparing the Incubators is difficult for several reasons: they have been operating for different (short) periods of time in different locations, with different business models. While incubator success can be better evaluated after 7-8 years, it should be possible to see trend differences between successful and less successful incubators after three years of operation. Table 6.1 summarises the performance of the Incubators against some selected key performance indicators drawn from the Pilot Evaluation. Other indicators listed in the Pilot Evaluation Report have not been presented because of problems with small sample size and difficulties in making comparisons.

Incubatee sustainability is usually measured by the survival rate three years after graduation, a point not yet reached by any Incubatee. Incubator sustainability, at this time, is highly dependent on further funding and/or a successful exit from an investment. The former is a matter to be considered by the Government and the latter is very difficult to assess.

In the longer term, a wider range of performance measures (discussed in Chapter 2) can be applied.

*Finding 5: A number of success factors have been used to evaluate the performance of the Incubators to date, including capital and in-kind contributions leveraged, Incubatee/graduate sustainability, the satisfaction of Incubatees with their incubation experience, and the extent to which Incubators have achieved self-sustaining operations. While there is some variation in performance between the Incubators, in the circumstances the overall results for the two Programs are good.*

Table 6.1

**COMPARISON OF INCUBATOR PERFORMANCE**

| Indicator   | Purpose  | Best performers in rank order                      |
|---|--|--|
| <b>Efficiency</b>   |  |  |
| Total Incubator support divided by Program Funds spent                                | Leverage of government funding                 | Playford, ADI, ICV, Epicorp                        |
| Support to Incubatees divided by Program funds spent (%)                              | Extent to which govt. funds went to Incubatees | InQbator, Epicorp, In-tellinc, BlueFire            |
| <b>Effectiveness</b>  |  |  |
| Incubatee funds raised divided by Program Funds spent                                 | Capital raised to date                         | Playford, A&B, ADI, InQbator                       |
| Increase in Incubatee & Graduate revenue divided by Program funds spent               | Increase in revenue (to date)                  | BlueFire, InQbator, In-tellinc, A&B                |
| Incubatees & Graduates who rated Incubator in-kind services as 'good' (% respondents) | Incubatee assessment of services provided      | BlueFire, EiR, Epicorp, InQbator (all rated equal) |
| <b>Utility</b>  |  |  |
| Incubatees & Graduates overall rating of Incubator as 'good' or better (%)            | Overall assessment by Incubatees and Graduates | InQbator, In-tellinc, Epicorp, BlueFire            |
| <b>Sustainability</b>   |  |  |
| No useful indicators at this time   |  |  |

Source: The Allen Consulting Group

## Chapter 7

# Conclusions and Findings Program Performance

### 7.1 The role of BITS and Intelligent Island Incubator Programs in the Innovation System

One of the special features of the BITS and Intelligent Island Incubator Programs is the way that they combine their assistance with early seed funding, based on the achievement of milestones. With the help of experienced Incubator managers, mentors and other business advisors, Incubators supported by the BITS and Intelligent Island Programs provide an *integrated* approach to helping start-ups to grow to the point where they can attract further investment. This makes them much more effective than other forms of government assistance in growing new internationally competitive ICT businesses.

The BITS and Intelligent Island Incubator Programs are uniquely positioned to assist start-up businesses. They provide assistance in relation to the establishment, planning and development of a business where such assistance is not available through other government programs designed to support innovation.

While business incubators often provide little more than low-cost office space, the BITS and Intelligent Island Incubators match specialised services with the particular needs of the individual ICT businesses, provide seed funding and assist in finding further investment.

There are only two other Australian Government programs that assist in the creation and growth of ICT start-ups — the COMET Program and, to a lesser extent, the Pre-seed Funds.<sup>37</sup> Other generally available programs are also relevant, encouraging venture capital (IIF Program) and supporting industrial R&D (R&D Start, R&D Tax Concession, R&D Rebate). The relationship of these support programs to the different stages of company development is illustrated in Figure 7.1, and discussed below.

#### *The Pre-seed Funds*

The Pre-seed Funds have only recently commenced operation. The assistance that they provide is limited to spin-offs from universities and public sector research agencies, enabling them to take research outcomes to a venture capital ready stage. As a consequence, very few of the BITS and Intelligent Island Incubatees are eligible for assistance from the Pre-seed Funds. Private sector fund managers operate the Pre-seed Funds and have commercial experience in developing new ventures.

The Pre-seed Funds do not provide the support that the BITS and Intelligent Island Incubators do in helping to establish and structure new businesses. Rather, the Pre-seed Funds are looking for opportunities that are ‘investment ready’ — that is, they have a business model capable of providing a growth path to the point where early investors can exit and obtain an appropriate return. While Pre-seed Funds can invest up to \$1m, it is believed that investments to date have been well below this figure.

<sup>37</sup> DITR, 2001, *Commonwealth and State Government Programs Supporting Innovation in Firms*, accessed at [www.industry.gov.au/library/content\\_programs.pdf](http://www.industry.gov.au/library/content_programs.pdf) on 21 September 2003.

*Venture Capital Measures*

The Innovation Investment Fund (IIF) Program is designed to encourage venture capital and operates on longer time scale, providing assistance over a 10-year period. Incubatees should be well positioned to attract investment from the IIFs once they have graduated. In addition as noted in the previous Chapter, recent Australian Government legislation allows the creation of venture capital funds structured as limited partnerships.

*COMET*

COMET provides assistance to firms via two streams — Tailored Assistance for Commercialisation (TAC) and Management Skills Development (MSD).

Under TAC, clients work with a Business Adviser to develop a tailored assistance plan to commercialise innovative products, processes or services. The majority of the strategies are designed to develop the management team, business plan, market research and intellectual property protection required to successfully commercialise an innovation, including securing equity funding.

The MSD stream is for individuals and companies whose immediate needs are management skills related to innovative practices and the financial management of commercialisation. They receive assistance to undertake existing management development programs. The MSD is only a minor element of COMET.

Figure 7.1

**ASSISTANCE FOR THE ESTABLISHMENT AND GROWTH OF NEW ICT BUSINESSES**

| Assistance                                      | Stages of Development |                   |                |                    |
|---|-----------------------|-------------------|----------------|--------------------|
|   | Startup               | Early Development | Expansion      | Later Stages       |
| Capital   |                       |                   | Pre-seed Funds |                    |
| Capital   |                       |                   |                | IIF's              |
| Capital, Advice & Business Development Services | BITS                  |                   |                |                    |
| Business Planning                               |                       | COMET             |                |                    |
| R&D   |                       |                   | R&D Rebate     |                    |
| R&D   |                       |                   |                | R&D Start          |
| R&D   |                       |                   |                | R&D Tax Concession |

Note: 1. Most BITS and Intelligent Island Incubatees are not eligible for Pre-seed Fund investment.  
 2. SBIP has not been shown because of its very small size.

Source: The Allen Consulting Group

Neither stream of the COMET Program involves a cash investment component, nor do they include the other features of business incubation provided by the BITS and Intelligent Island Incubator Programs. The average COMET grant is approximately \$53,000.

#### *Small Business Incubator Program*

The Small Business Incubator Program (SBIP) provides funding for non-profit organisations to provide premises, business advice, shared services and other support to early growth companies. Program funding has been approximately \$4-5m per annum although expenditure in 2002-03 was only \$2.6m. The Program was designed as an employment creation initiative targeting the unemployed. It supports incubators across Australia, particularly incubators in rural areas.

SBIP Funds are available to help cover the costs of setting up an incubator. In certain circumstances, existing incubators may apply for enhancement funding. Three types of grants are available under the Small Business Incubator Program: Feasibility Study Grants up to \$25,000, Establishment Grants up to \$500,000, and Enhancement Grants up to \$100,000.

#### *R&D Support*

The R&D Start Program provides 50 per cent taxable grants for industrial research and development. Competition for these grants is strong and recent start-ups find it difficult to obtain this funding. The R&D Tax Concession provides a deduction (125 per cent, or in some cases 175 per cent of eligible costs) to established companies undertaking R&D. The R&D Tax Offset (Rebate) has been introduced since the BITS Incubator Program commenced. The Rebate is designed to meet the needs of smaller companies with R&D expenditure up to \$1m per year.

#### *Analysis*

These Programs are all quite different to the BITS and Intelligent Island Incubator Programs. They generally address a single need (eg R&D) rather than providing the comprehensive integrated assistance available through the BITS and Intelligent Island Incubator Programs. The BITS and Intelligent Island Incubator Programs provide early stage finance, assistance with business planning, valuable networks, business coaching, mentoring and channels to markets. The Incubators provide multi-faceted assistance and are one-stop shops for ICT start-ups.

In terms of assistance with investment, there are no other government programs in Australia that fill the gap between the seeds of a new ICT idea and the level at which venture capital sources will invest. Importantly, stakeholders consulted during this evaluation believe that the funding gap argument for the Programs is as relevant now as it was in June 2000. In this way, the Programs play a significant role in the national innovation system.

*Finding 6: The BITS and Intelligent Island Incubator Programs are uniquely positioned to assist start-up businesses. They provide assistance in relation to the establishment, planning, development and financing of ICT, addressing the gap between the seeds of a new ICT idea and the level at which venture capital sources will invest. There are no other government assistance programs in Australia that provide such broad-based support. The funding gap which start-up businesses face is as relevant now as it was in June 2000. The BITS and Intelligent Island Incubator Programs play a significant role in the national innovation system.*

## 7.2 Outcomes of the BITS and Intelligent Island Programs

In spite of the difficulties in the ICT investment climate since the 'tech wreck', the Incubators have been able to assist many new ICT businesses to get started. The average period of Incubator operation is only three years. In this time, 3,659 applicants for assistance have been screened. Some 267 companies have received incubation services and 127 have graduated.

### *Capital leveraged*

For their own operations, the Incubators have obtained approximately \$20m in funding from other sources.

In addition, the Incubators have assisted their Incubatees to obtain funds from business angels (nearly \$26m), venture capitalists (nearly \$46m) and from other sources (including government grants) (\$12m) bringing the total for non-BITS funds raised for Incubatees to \$84m.

### *In-kind contributions leveraged*

The Incubators have been able to leverage more than \$10.5m in in-kind contributions (estimated) in the form of advice, equipment, or premises. These contributions have been provided by lawyers, patent attorneys and other service providers who have a relationship with the Incubators. State Governments and research organisations have also contributed in this way.

### *Incubatee/graduate sustainability*

In relation to sustainability, on the basis of the survey responses the prospects look promising for many of the BITS and Intelligent Island Incubatees.

The average period of incubation for the 100 Incubatees that responded to the survey was only 13.5 months. Even in this very short period, 61 per cent of Incubatees reported annual revenues averaging \$386,591 and 68 per cent reported growth in employment averaging 6.2 per cent in 2002-03. Some 24 per cent of Incubatees reported that they had commenced exporting with an average value of \$380,574 in 2002-3.

For the Programs overall, it is estimated by the Incubators that their Incubatees have achieved the following outcomes.

- Employment has risen from an average of 3.3 FTE per Incubatee in 2000-01 to 5.3 FTE per Incubatee in 2002-03. Total Incubatee employment at 30 June 2003 was 726 FTE.
- Total annual revenue has risen from \$11.3m in 2000-01 to \$37m in 2002-03.
- Total annual export revenue has risen from \$1m in 2000-01 to \$6.7m in 2002-03.

While these are early results and can be expected to improve over time, they are nonetheless impressive. This is especially so considering the extremely short time frame in which they have been achieved and the difficulty of the ICT business climate, as noted above.

Survival rates of Incubatees and graduates can provide a measure of how well an Incubator has done its job — typically, these survival rates are measured at three years *after* graduation. The BITS and Intelligent Island Incubator Programs currently have no graduates of this age. There have also been a number of withdrawals from the Programs but these firms may continue to trade without the help of the Incubator.

Another approach to estimating ICT start-up survival rates would be to compare the performance of BITS and Intelligent Island Incubatees and graduates with other similar companies that have not received incubation assistance. However, this kind of data is not available in Australia, which makes it challenging to compare results. The ABS reported in 1997 that two-thirds of new businesses (across all industry sectors) are still operating after five years of trading. It is reasonable to expect that the figure for ICT start-ups is likely to be much lower than this because they are developing early stage technologies, and they are operating in the much riskier ICT industry sector. The impacts of the ‘tech wreck’ on the ICT sector would have made the chances of success for these businesses even lower.

To date, around 80 per cent of graduates that received significant assistance are still trading (that is, those that received greater than \$50,000 of investment). Therefore, at this early stage, the BITS and Intelligent Island Incubatees appear to have a lower failure rate than other Australian start-ups of similar age. A more stringent test would be to test the number of them still trading after five years. The outcome for graduates that received limited assistance is not clear because a majority of them are not in contact with their Incubator and their current trading status is unknown.

While some Incubatees may have achieved a degree of sustainability, in terms of the outcomes reported above, without the involvement of the Incubators, it is clear from the survey responses that the Incubators have played a key role in the majority of Incubatee companies. While a number of them would probably still exist without the Incubators’ assistance, they would not have progressed as far or as quickly, and many probably owe their existence to the BITS and Intelligent Island Incubator Programs.

#### *Satisfaction of Incubatees*

The majority of Incubatees are happy with the performance of their Incubators. The survey results show that 80 per cent of Incubatees rated their Incubator as ‘good’ or better, while over half rated them as ‘very good’ or ‘excellent’. Many of the Incubatees noted that the only real barrier to them not progressing faster was a lack of further capital injections. The most significant concern raised by surveyed Incubatees (not across all Incubators) was the feeling that, in some cases, they were compelled to purchase services on a charge back basis from their Incubator.

#### *Self-sustaining Incubator operations*

There have been very few investment exits achieved so far and as a result none of the Incubators have achieved self-sustaining operations to date. In addition, none of them believe that they could maintain their activities at current levels when BITS Incubator Program funding is scheduled to cease on 30 June 2004.

While most Incubators are confident of moving towards self-sustaining operations, they estimate that it would take at least until June 2006 for the majority to have some chance of being self-sustaining. Most have sensibly operated with ‘one eye

on the future' and made genuine efforts to diversify their sources of funding and revenues.

The ultimate key to self-sustaining operations, however, is to achieve investment exits. Given their short period of operation and the business climate in which they have operated, it is not reasonable to expect that any of the Incubators will have achieved self-sustaining operations by 30 June 2004. In order to achieve exits, there is a requirement that Incubators have a steady flow of Incubatees and are able to achieve a critical mass of business opportunities. If some further assistance is provided to assist with this flow, it is likely that a number of them will create substantially self-sustaining operations in the future.

#### *Skilled ICT and Incubator managers*

The BITS and Intelligent Island Incubator Programs have also produced hundreds of start up ICT managers who have either built an SME or have gone through a process (including structured feedback in many cases) that has equipped them to either grow their business further or be much better prepared to commercialise their next idea. While some of these ICT managers would have probably pursued their ideas without the help of the BITS and Intelligent Island Incubator Programs, it is clear that many of them were poorly equipped to take their ideas to the next stage, and therefore owe their success solely to the Programs.

In relation to those that would have pursued their ideas in any event, the Programs have undoubtedly accelerated the process of skills acquisition. The discipline imposed by the Incubators, including the stringent investment milestones they have set, has forced many Incubatee managers to be far more focused and resolute than they would have been otherwise.

The BITS and Intelligent Island Incubator Programs have provided Australia with a pool of skilled individuals with 2-3 years experience in building and operating ICT business incubators. Australia should seek to build on this experience.

*Finding 7: The BITS and Intelligent Island Incubator Programs have produced hundreds of start up ICT managers who have gone through the process of starting a business and/or have gone through processes that have equipped them to grow their business to the point of achieving self-sustaining growth in revenues. While the Programs have accelerated the process of skills acquisition for some, many others owe their success to the Programs – which have also created a pool of skilled individuals with 2-3 years experience in building and operating ICT business incubators.*

#### *Overall*

The early outcomes to date indicate that the BITS and Intelligent Island Incubators have been, by and large, very successful, especially given their short period of operation and the business climate in which they have operated. With further funding, the Incubators can be expected to continue to be successful.

*Finding 8: Government assistance provided through the BITS and Intelligent Island Incubators has enabled Incubatees to start and develop new businesses as well as create additional ICT jobs, revenues and exports. Considering the environment in which they have operated, the Incubators have generated outcomes to date that are impressive, especially given their short period of operation and the business climate in which they have operated.*

### 7.3 International comparisons

Any comparisons of the BITS and Intelligent Island Incubators in this evaluation with international survey results need to recognise the short time that the Australian Incubators have been operating. Each of the Incubators took some time to establish their operations, reducing their average operating period to just on three years. Given average incubation periods in other countries of three to four years, the fact that the Programs have any graduates at this time is quite an achievement. It would be unreasonable to expect the Incubators to fully match the performance figures reported for established international incubators at this time, given that their average age is upward of eight years.<sup>38</sup>

The number of Incubatees being serviced by BITS and Intelligent Island Incubators is small, even by the standards of new economy incubators, reflecting the limited resources available to the BITS and Intelligent Island Incubators. The average BITS and Intelligent Island Incubator staffing levels are also significantly lower than their European and North American counterparts. This suggests that, with more resources, BITS and Intelligent Island Incubators could achieve economies of scale, which would help to move towards self-sustaining operations.

At this time, Incubatee failure rates appear to be lower than those in other countries. BITS and Intelligent Island Incubatees priorities for assistance from their Incubators are also comparable with their overseas counterparts. Employment, revenue and export growth comparisons with overseas surveys are not valid at this early stage. The assessment of BITS and Intelligent Island Incubators by their Incubatees is broadly comparable with overseas experience.

The problem of incubator size and scale is not unique to BITS and Intelligent Island Incubators. It has also been observed in 13 out of 18 general business incubators in Victoria. In relation to small incubators, that study noted that;

‘as they come to the end of their initial funding, their financial vulnerability will increase, and management inputs will either be diverted away from tenant assistance to revenue raising, or will be reduced to cut costs’.

Finney Whelan International/Allen Consulting Group/Acuity Consulting, 1998, *Building Victoria's Smart Infrastructure – A review of Victoria's Technology Parks and Business Incubators*. Prepared for The Premier's Science, Engineering and Technology Task Force, Melbourne.

Salaries of staff are the most significant cost to BITS and Intelligent Island Incubators and the numbers of staff reflect the scale of the Incubator. As noted above, the BITS and Intelligent Island Incubators are, on average, small by international standards. As a consequence, on average the Incubators cannot at this time employ sufficient staff to provide a level of activity comparable with their international counterparts.

Mature ICT incubator markets such as the USA have an added advantage of proximity to clusters of ICT industry activity. This is a particular challenge for those Incubators not located on Australia's eastern seaboard.

<sup>38</sup> Centre for Strategy & Evaluation Services, 2002, *Benchmarking of Business Incubators*. Final report for the European Commission Enterprise Directorate-General, accessed on 14 January 2003 at [http://europa.eu.int/comm/enterprise/entrepreneurship/support\\_measures/incubators/summary\\_benchmarking\\_bi\\_2002.pdf](http://europa.eu.int/comm/enterprise/entrepreneurship/support_measures/incubators/summary_benchmarking_bi_2002.pdf)

*Finding 9: The BITS and Intelligent Island Incubators are smaller and have operated for a much shorter period than their overseas counterparts, making comparisons problematic. A particular challenge for those Incubators not located on Australia's eastern seaboard is that they are not situated close to clusters of ICT industry activity.*

## Chapter 8

# Recommendations

### ***Should the Incubators Receive Further Funding?***

One way of deciding whether further funding should be provided is to examine how the Programs are performing against their objectives.

The objectives of the Incubator Programs are to:

- improve the rate of commercialisation of ICT ideas, research and development;
- assist eligible Incubator firms to reach their full potential;
- play a significant role in the national innovation system; and
- have incubation centres become viable in the medium term without ongoing support from the Program.

While it has not been possible to establish a precise measured improvement in the rate of commercialisation of ideas, research and development, it is clear that many of the Incubatees involved in these activities owe their existence to the Programs, and others that might exist now even without incubation support, would not have progressed as far or as quickly without the Programs — that is, their rate of development has been accelerated. The comments received from Incubatees, Incubators and other stakeholders uniformly suggest that many of the Incubatees that are now building viable businesses would have had little chance of progressing their ICT ideas were it not for the assistance received through the Programs. Whilst the seeds of an idea were present, they would in most cases have failed to germinate into viable businesses without the support of the BITS and Intelligent Island Incubator Programs.

There is evidence that the Incubators have helped the majority of their Incubatees to reach their full potential, and most Incubatees fully appreciate the added value of their incubation experience.

As noted earlier, there are no other Australian Government programs that adequately fill the gap between the seeds of a new ICT idea and the level at which venture capital sources will invest. In this way, the BITS and Intelligent Island Incubator Programs play a significant role in the national innovation system.

The period in during which the Incubators have operated has been exceptionally unfavourable to the establishment and growth of new ICT businesses, and early stage capital investment has been very scarce. As a result, none of the Incubators are currently viable without ongoing support from the Programs. While many of the Incubators are well placed to be viable and substantially self-sustaining over the next few years, this will not be achieved without further Government assistance. The BITS and Intelligent Island Incubators have been in operation on average for only three years. Overseas experience shows that this is well short of the time required for Incubators to reach a point where they are receiving a steady stream of revenue from their investments.

The experience in mature ICT markets such as the USA and the UK is that 75 per cent of business incubators (of all types) require continuing government assistance. Furthermore, the 25 per cent of Incubators that are successful without direct funding assistance would not be viable, were it not for sponsorship or indirect subsidies provided by (or at least with strong links to) local and or regional governments, universities or government laboratories.

If further funding is not provided at this time, it is probable that most of the Incubators will not be viable, and a number of Incubatees currently receiving assistance will fail. This will result in a write off of most of the Australian Government's investment in the BITS and Intelligent Island Programs.

In addition, if the BITS and Intelligent Island Incubator Programs are not continued in some form, Australia will be unable to build a vibrant ICT sector sustained by a healthy flow of viable new businesses and entrepreneurs. While early stage concepts and products of the kind that have been supported by the BITS and Intelligent Island Programs will still be generated, the number of these will be substantially reduced — for many of the Incubatees that responded to the questionnaire, the BITS and Intelligent Island Incubator Programs are 'the only game in town', especially in relation to the regional Incubator operations.

The BITS and Intelligent Island Incubator Programs play an important role in partly filling a gap at the start-up point of the innovation cycle. Even with the assistance and investment provided by the Incubators, there remains a gap between the funds provided by BITS Incubators and business angels, and the level at which venture capital sources will invest.

Without further assistance, many of the companies helped by the Incubators will not survive long enough to become self-sustaining or to attract venture capital and other investment. While some of them are demonstrating solid revenue growth, and a few are even generating profits, most still require continued assistance to survive. Very few of the Incubators will be able to continue to provide the basic range of services normally associated with business incubation.

As a consequence of the state of the ICT market, there is a risk that the BITS and Intelligent Island Incubators will be forced to make early exits from their investments in order to survive.

*Finding 10: The BITS and Intelligent Island Incubators have performed well in terms of the objectives of the Programs, particularly given the short period of their operation and the prevailing business conditions. Without a further period of assistance, however, it is probable that most of the Incubators will not be viable, and a number of promising Incubatees currently receiving assistance will fail. This will result in a write off of most of the Australian Government's investment in the BITS and Intelligent Island Incubator Programs.*

*Recommendation 1: The BITS and Intelligent Island Incubators Programs have achieved encouraging results to date and should receive further funding.*

***How long should the BITS and Intelligent Island Incubator Programs run for?***

This evaluation demonstrates that the BITS and Intelligent Island Programs need more time to run their course. The Programs were conceived and designed prior to the ‘tech wreck’. At this time, there was more business angel and venture capital support available and the Incubators believed that they could become largely self-sufficient through exits from successful investments.

During this evaluation, Incubator managers argued for more time to prove their incubation models. Finance practitioners such as venture capitalists, with no direct stake in the Incubators, agreed that seven to eight years would be the minimum time required for the Incubators to reach a point where they were receiving real revenues from their investments. The international literature on business incubator models supports the view that six to eight years in ‘normal’ times would be required to establish a viable business Incubator.

Consequently, there is a sound case for the BITS and Intelligent Island Programs to be provided with at least an additional four years of funding in order to give the better performing Incubators the opportunity to demonstrate success.

*Recommendation 2: The BITS and Intelligent Island Incubators Programs should be funded for at least an additional four years to give the better performing Incubators the opportunity to demonstrate success.*

***How much further funding is required?***

The amount of additional funding for the BITS and Intelligent Island Incubator Programs depends on which option is chosen.

The original funding of the BITS Incubator Program was \$78m over four years and the funding of the Intelligent Island Incubator Program was \$8m over a similar period. If all the Incubators were to be provided with further funding a similar investment would be involved, although some of the original establishment costs would not recur and running (or operational) costs could be minimised through a requirement that operational costs are provided on a matching basis from other sources. The requirement to cover some of the running costs from other sources reflects the fact that many of the benefits of incubation are localised. The contribution of the South Australian Government to Playford Capital Pty Ltd is a reflection of this and could provide a model from which further funding mechanisms could be designed. This would also mean that more of the Australian Government funds could be dedicated to capital expenditures – that is, direct investment into the Incubatees.

In providing any further assistance to Incubators on the basis of performance, consideration should be given to the usefulness and value of a regional presence in growing new ICT businesses, the particular challenges that have been faced by the regional Incubators by virtue of their distance from the major eastern Australian ICT markets, and their limited access to the required supporting infrastructure.

***What are the principles on which further funding should be based?***

On the basis of the findings of this evaluation, a number of principles have been developed that should be used as a basis for any further funding of the BITS and Intelligent Island Incubators.

- There should be a competitive process for further funding limited to the existing Incubators. This reflects the experimental nature of the Programs and the finding that not enough time has been provided for the Incubators to prove their models in the business conditions that have prevailed.
- Incubators should be selected or retained on the basis of the value added that they can demonstrate. The Incubators need to demonstrate that they are able to do more than simply provide accommodation or seed capital.
- Requests for funding should separately identify basic incubator operating costs and funds earmarked for investment in Incubatees. This would ensure that Incubatees receive an appropriate and identifiable amount of cash investment from their Incubators.
- Incubatees should be free to purchase the professional services they need either from their Incubator or from other sources. By giving Incubatees a choice of service providers, the Incubators will have to convince Incubatees that they can provide value for money and the Incubatees will have more ownership of the services purchased.
- The Incubators should use their limited resources in ways which maximises their impact. BITS and Intelligent Island Incubator Program funds should therefore not be used to provide business training courses that are available from a local TAFE or university. If the Incubators do wish to offer such courses, they should obtain funds for this purpose from other sources, such as other levels of government.

*Recommendation 3: Further funding should be based on a competitive process where Incubators demonstrate the value added they can bring to Incubatees. Basic Incubator operating costs and funds earmarked for investment in Incubatees should be separately identified. Incubatees should also be free to purchase the professional services they need either from their Incubator or from other sources. Where business training courses are available from local TAFEs or universities, they should not be provided using BITS funds.*

## *Appendix A*

### **CONNECT, San Diego**

In a typical year, CONNECT assists between 100 and 200 companies per year through a variety of programs. With CONNECT's virtual incubation model, the throughput can be much higher than the typical USA physical incubator program and much higher than the throughput of a typical BITS incubator. The higher the throughput and the higher the quality of companies assisted, the greater the acceleration in building an entrepreneurial high tech community and the higher the likelihood of nurturing a high tech industry cluster in a region.

CONNECT operates two Financial Forums per year - a High Technology Financial Forum, and a Life Sciences Financial Forum. Over 100 companies apply. The forty finalists chosen for each Forum and each finalist firm receives personalized coaching for practice runs in front of a volunteer screening panel of distinguished business leaders. Some 25 companies are chosen to present at the Forum itself. Between 1995 and 2001, CONNECT's Financial Forum companies have raised over \$US1.44 billion in the year following their participation with the average being \$US11.43 million per company

CONNECT also operates a Springboard Program for Start-up Companies and Entrepreneurs. Some 50-60 companies/entrepreneurs apply, all receive some mentoring/coaching assistance from CONNECT staff. Some companies drop out. Companies receive intensive one-on-one mentoring by CONNECT staff over the course of 10-12 weeks (the length of time depends on the company, the issues that need to be addressed in the business plan and staff availability to schedule meetings). At the end of this period, approximately 20 companies/entrepreneurs graduate. Graduation involves presenting the final business plan in front of a panel of 10-12 local business leaders specifically chosen for their expertise in the company's industry sector (typically a mix of venture capitalists, angel investors, IP lawyers, other high tech business service providers, and corporate executives). Between 1995 and 2002, Springboard companies raised over \$US575.6 million with the average being \$US9.37 million, per company

CONNECT's Most Innovative Products of the Year Award attracts 100 nominees submitted by the local business community (companies must be nominated). All nominees are judged by a volunteer panel of distinguished business leaders. One winner is chosen in each of seven categories.

CONNECT does not provide incubatees with funding but is extremely active in cultivating relationships with the local and regional (Bay Area) venture capital community. Some of the new programs that have developed in the past few years include an on-going relationship with the San Diego chapter of the Tech Coast Angels (TCA). CONNECT staff provide front-end administrative support for Tech Coast Angel activities and in return, CONNECT mentored companies have an opportunity to present their business plans to TCA.

## Appendix B

### Incubatee Survey Results

*This Appendix provides detailed results of the Incubatee Survey in tabular form.*

BITS Program Evaluation Surveys were sent out to all Incubatees and Graduates of the Program via their incubators. A total of 100 responses were received from Incubatees, from a total of 254 surveys sent out by Incubators (a response rate of 39 per cent). Two respondents to the survey indicated that they were offered a place with an incubator but did not accept the offer.

In the completed surveys, some respondents did not provide any answer to individual questions, which in this Appendix have been recorded as 'no response'. Due to confidentiality concerns the full set of comments provided in the surveys are not documented here, though in some cases the responses provided have been summarised and collated as to provide some information about the trend of responses.

#### Question 1

This Question asked for name and contact details of respondents. Individual responses remain commercial-in-confidence. Respondents were asked to identify their incubator. Table B.1 provides the breakdown of survey responses by incubator.

Table B.1

#### INCUBATEES RESPONSES TO THE SURVEY BY INCUBATOR

| Incubator    | State (1) | Total Number of responses | Response rate of Incubatees receiving over \$50,000 (%) | Response rate of Incubatees receiving under \$50,000 (%) |
|--------------|-----------|---------------------------|---|--|
| ADI          | Vic       | 10                        | 57  | 3  |
| A&B          | NSW       | 7                         | 67  | 5  |
| BlueFire     | NSW       | 7                         | 64  | 0  |
| EiR          | WA        | 11                        | 60  | 71   |
| Epicorp      | ACT       | 10                        | 67  | 14   |
| ICV          | Vic       | 19                        | 29  | 83   |
| InQbator     | Qld       | 7                         | 70  | NA   |
| In-tellinc   | Tas       | 12                        | 100   | 100  |
| Item3        | NSW       | 5                         | 45  | NA   |
| OiT          | NT        | 3                         | 25  | 17   |
| Playford     | SA        | 9                         | 64  | 33   |
| <b>TOTAL</b> |           | <b>100</b>                | <b>55</b>   | <b>17</b>  |

Note: This column shows the State or Territory in which the Incubator has its headquarters. Some incubators provide virtual incubation more widely across Australia.

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 2**

*On what date did your Incubation commence?*

Table A.2 provides a summary of the starting date for incubation for those Incubatees who responded to the survey.

Table B.2

**STARTING DATE FOR INCUBATEES WHO RESPONDED TO THE SURVEY**

|                           | Percentage |
|---------------------------|------------|
| July 1999 - December 1999 | 1          |
| January 2000 - June 2000  | 3          |
| July 2000 - December 2000 | 8          |
| January 2001 - June 2001  | 13         |
| July 2001 - December 2001 | 15         |
| January 2002 - June 2002  | 27         |
| July 2002 - December 2002 | 13         |
| January 2003 - June 2003  | 14         |
| July 2003                 | 2          |
| No response               | 4          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 3**

*If you have graduated from incubation, what was your date of graduation?*

Of the 100 responses received from Incubatees, 36 indicated that they had graduated from incubation. Table A.3 provides details on the date of graduation for these graduates.

Table B.3

**GRADUATION DATE FOR INCUBATEES**

|                           | Number of Graduates |
|---------------------------|---------------------|
| January 2001 – June 2001  | 2                   |
| July 2001 – December 2001 | 4                   |
| January 2002 – June 2002  | 9                   |
| July 2002 – December 2002 | 5                   |
| January 2003 – July 2003  | 16                  |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 4**

*If you are a 'withdrawal' from an Incubator, please indicate the reason for your withdrawal.*

Of the 100 Incubatees who responded to the survey, 14 had withdrawn from incubation. Table A.4 shows the reasons given for withdrawal by Incubatees. Some Incubatees gave more than one reason for withdrawal.

Table B.4

**REASONS FOR WITHDRAWAL FROM INCUBATION**

|  | Number of incubatees |
|--|----------------------|
| Lack of commercial prospects           | 4                    |
| Disagreement with incubator management | 4                    |
| Inadequate funding                     | 5                    |
| Market for product/service not ready   | 3                    |
| Other                                  | 6                    |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Under 'Other', the following was specified:

- Incubator wanted too much — overvalued their services.
- Failed to meet milestones. Failed to create team. Similar businesses having trouble making their businesses viable.
- Could not afford to stay.
- A dispute regarding incubator requirements for further equity to allow us to continue in the program.

**Question 5**

*What is the total of BITS funds (cash) you have actually received from your Incubator up to 30 June 2003?*

Of the 100 responses received, 95 provided details of the total BITS funds (cash) received from their incubator. The total amount of BITS cash funds received was \$18,541,284, an average of \$185,412 per Incubatee. Table A.5 provides details on the distribution of funds across Incubatees.

Table B.5

**FUNDS RECEIVED FROM INCUBATOR (PERCENTAGE OF INCUBATEES)**

|                       | Percentage |
|-----------------------|------------|
| \$0                   | 5          |
| \$1 – \$10,000        | 10         |
| \$10,001 – \$20,000   | 4          |
| \$20,001 – \$50,000   | 13         |
| \$50,001 – \$100,000  | 8          |
| \$100,001 – \$150,000 | 12         |
| \$150,000 – \$200,000 | 5          |
| \$200,001 – \$300,000 | 10         |
| \$300,001 – \$400,000 | 9          |
| \$400,001 – \$500,000 | 12         |
| \$500,001 – \$600,000 | 7          |
| No response           | 5          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 6**

*What is the total of BITS funds (cash) you have yet to receive from your Incubator (possibly subject to milestones)?*

A total of 23 Incubatees indicated that there were funds that they were yet to receive from their incubator. The total amount still to be received was \$1,572,668, an average of \$68,376 per Incubatee.

**Question 7**

*What is the approximate total value of any in-kind contributions provided by or through your Incubator that you have actually received to 30 June 2003?*

Of the 100 Incubatees who responded to the survey, 81 indicated that they had received in-kind contributions from their Incubator. Table A.6 shows the distribution of the value of in-kind contributions received by these Incubatees.

**Question 8**

*What is the approximate total value of any in-kind contributions you have actually received to 30 June 2003 from sources other than your Incubator?*

A total of 76 Incubatees indicated that they received in-kind contributions from sources other than their incubator. Table A.6 provides the distribution of the value of in-kind contributions received by Incubatees.

Table B.6

**VALUE OF IN-KIND CONTRIBUTIONS FROM INCUBATOR**

| Value of in-kind contribution | From Incubator (%) | From sources outside the Incubator (%) |
|-------------------------------|--------------------|--|
| \$0                           | 15                 | 21                                     |
| \$0-\$50,000                  | 59                 | 55                                     |
| \$50,000-\$100,000            | 8                  | 3                                      |
| \$100,000-\$150,000           | 6                  | 10                                     |
| \$150,000-\$200,000           | 3                  | 2                                      |
| \$200,000-\$250,000           | 2                  | 5                                      |
| \$250,000-\$300,000           | 0                  | 0                                      |
| \$300,000-\$350,000           | 4                  | 2                                      |
| \$350,000-\$400,000           | 3                  | 0                                      |
| \$400,000-\$450,000           | 0                  | 1                                      |
| \$450,000-\$500,000           | 0                  | 0                                      |
| Greater than \$500,000        | 0                  | 1                                      |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 9**

*What is the total of other (that is, non BITS) funds that you have actually received for any purposes to 30 June 2003?*

Tables A.7 to A.9 show the percentages of Incubatees who were able to secure funding through loans, grants and equity from sources outside the BITS Program, and the total funds received by Incubatees.

Table B.7

**LOANS RECEIVED BY INCUBATEES**

| Source of Loan                 | Percentage of Incubatees | Total funds received (\$) |
|--------------------------------|--------------------------|---------------------------|
| Non-BITS funds from Incubator  | 6                        | 145,000                   |
| Shareholders                   | 13                       | 900,000                   |
| Own funds                      | 17                       | 1,960,633                 |
| Australian Government          | 5                        | 985,000                   |
| State and Territory Government | 1                        | 10,000                    |
| Other sources                  | 3                        | 1,380,000                 |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.8

**GRANTS RECEIVED BY INCUBATEES**

| Source of Grant                | Percentage | Total funds received (\$) |
|--------------------------------|------------|---------------------------|
| Non-BITS funds from Incubator  | 1          | 20,000                    |
| Shareholders                   | 1          | 79,000                    |
| Own funds                      | 5          | 1,978,000                 |
| Australian Government          | 31         | 8,768,070                 |
| State and Territory Government | 13         | 836,086                   |
| Other sources                  | 7          | 727,000                   |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.9

**EQUITY RECEIVED BY INCUBATEES**

| Source of Equity                 | Percentage | Total funds received (\$) |
|----------------------------------|------------|---------------------------|
| Non-BITS funds from Incubator    | 7          | 9,706,666                 |
| Shareholders                     | 35         | 29,847,267                |
| Own funds                        | 28         | 10,582,150                |
| Australian Government (non-BITS) | 0          | 0                         |
| State and Territory Government   | 0          | 0                         |
| Other sources                    | 3          | 9,050,000                 |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 10**

*What is the ownership of your current equity?*

Of the 100 responses received, 95 Incubatees provided details of the ownership of the equity of their company. Table A.11 provides details of the proportion of Incubatee companies with equity ownership across the range of categories, and the average share of equity for each category.

Table B.10

**CURRENT OWNERSHIP OF EQUITY FOR INCUBATEES**

|                     | Percentage | Average share of equity (%) |
|---------------------|------------|-----------------------------|
| Yourself            | 84         | 58                          |
| BITS Incubator      | 79         | 18                          |
| Business Angels     | 22         | 23                          |
| Venture capitalists | 19         | 30                          |
| Family and friends  | 21         | 18                          |
| Employees           | 10         | 10                          |
| Founders            | 5          | 32                          |
| Partner             | 3          | 20                          |
| Parent company      | 1          | 83                          |
| Private investors   | 2          | 14                          |
| Directors           | 5          | 70                          |
| Not specified       | 6          | 38                          |
| Other               | 9          | 38                          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Under ‘Other’ the following were specified:

- cancer research centre;
- owned by contractor in return for services;
- source of IP;
- individuals and companies; and
- convertible note holders.

A further six incubatees did not specify the ownership of equity identified under ‘Other’.

**Question 11**

*Does your Incubator hold options in your company?*

Table A.12 provides details of the proportion of Incubatees who have options held in their company by their Incubator.

Table B.11

**INCUBATOR OPTIONS**

| Does a BITS Incubator hold options in your company? | Percentage |
|---|------------|
| Yes   | 13         |
| No  | 83         |
| No response   | 4          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Those Incubatees who indicated that their Incubator does hold options in their company were asked to provide details of the number of options held, the timing of the exercise of the options and the exercise price. Individual responses to this question remain commercial-in-confidence.

### **Question 12**

*What are the major products/services which your company provides?*

Responses provided under this category remain commercial-in-confidence. The responses were used to confirm the answers to Question 13.

### **Question 13**

*How would you classify your company?*

Incubatees were provided with a diagram illustrating classifications within the information and communications technology industry. Incubatees were asked to indicate which category their company fitted into. Table A.13 shows the distribution of incubatees across all categories. Some incubatees chose more than one classification for their company.

Table B.12

#### **CLASSIFICATION OF INCUBATEES**

|   | <b>Number of Incubatees</b> |
|---|-----------------------------|
| <b>Communications Services</b>                  |                             |
| Basic Telephony Services                        | 0                           |
| Call/Telephony Services                         | 0                           |
| Basic Carriage and Transmission                 | 0                           |
| Leased Line and PSDN services                   | 1                           |
| <b>Information Services</b>                     |                             |
| Higher Level and Network Services               | 11                          |
| Professional Services                           | 13                          |
| Network and Services                            | 6                           |
| Computer, Communications and Software services  | 11                          |
| <b>Information and Communications Equipment</b> |                             |
| Line, Transmission and Broadcasting Equipment   | 3                           |
| Switch, LAN/WAN and data Equipment              | 3                           |
| Terminal and Peripheral Equipment               | 3                           |
| Computer Equipment                              | 3                           |
| <b>Information Products</b>                     |                             |
| Network Software                                | 4                           |
| Packaged Software                               | 34                          |
| Systems Software                                | 8                           |
| Networked Content                               | 21                          |
| <b>No response</b>                              | <b>6</b>                    |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 14**

Please provide the information requested below relating to your company's progress.

Incubatees were asked to provide estimates of their company's revenue, exports and profit (if any) and employment for the last three financial years. Tables A.14 to A.17 provide details of the responses provided.

Table B.13

**ANNUAL REVENUE FOR INCUBATEES (2000-01 TO 2002-03)**

|                           | 2000-01<br>(%) | 2001-02<br>(%) | 2002-03<br>(%) |
|---------------------------|----------------|----------------|----------------|
| \$0                       | 12             | 10             | 9              |
| \$1 – \$50,000            | 10             | 12             | 15             |
| \$50,000 – \$100,000      | 3              | 5              | 9              |
| \$100,001 – \$200,000     | 3              | 8              | 8              |
| \$200,001 – \$400,000     | 1              | 5              | 14             |
| \$400,001 – \$600,000     | 2              | 7              | 2              |
| \$600,001 – \$800,000     | 3              | 1              | 5              |
| \$800,001 – \$1,000,000   | 0              | 3              | 1              |
| \$1,000,001 – \$2,000,000 | 3              | 3              | 6              |
| \$2,000,001 – \$2,500,000 | 0              | 0              | 1              |
| Not applicable            | 17             | 11             | 2              |
| No response               | 46             | 35             | 28             |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.14

**VALUE OF EXPORTS BY INCUBATEES (2000-01 TO 2002-03)**

|                           | 2000-01<br>(%) | 2001-02<br>(%) | 2002-03<br>(%) |
|---------------------------|----------------|----------------|----------------|
| \$0                       | 26             | 14             | 18             |
| \$1 – \$50,000            | 2              | 6              | 10             |
| \$50,001 – \$100,000      | 0              | 2              | 3              |
| \$100,001 – \$200,000     | 0              | 0              | 2              |
| \$200,001 – \$300,000     | 0              | 1              | 1              |
| \$300,001 – \$400,000     | 0              | 2              | 1              |
| \$400,001 – \$500,000     | 0              | 0              | 1              |
| \$500,001 – \$1,000,000   | 0              | 1              | 3              |
| \$1,000,001 – \$1,500,000 | 1              | 0              | 2              |
| \$1,500,001 – \$2,000,000 | 0              | 1              | 1              |
| Not applicable            | 15             | 10             | 2              |
| No response               | 56             | 63             | 56             |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.15

**PROFITS FOR INCUBATEES (2000-01 TO 2002-03)**

|                         | 2000-01<br>(%) | 2001-02<br>(%) | 2002-03<br>(%) |
|-------------------------|----------------|----------------|----------------|
| \$0                     | 19             | 19             | 27             |
| \$1-\$50,000            | 0              | 1              | 5              |
| \$50,001 - \$100,000    | 1              | 2              | 3              |
| \$100,001 - \$200,000   | 0              | 0              | 1              |
| \$200,000 - \$500,000   | 1              | 0              | 1              |
| \$500,001 - \$1,000,000 | 0              | 1              | 0              |
| Not Applicable          | 13             | 10             | 3              |
| No Response             | 66             | 67             | 60             |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.16

**EMPLOYMENT FOR INCUBATEES (2000-01 TO 2002-03)**

| Number of employees | 2000-01<br>(%) | 2001-02<br>(%) | 2002-03<br>(%) |
|---------------------|----------------|----------------|----------------|
| 0                   | 4              | 4              | 6              |
| 1                   | 7              | 4              | 7              |
| 2                   | 10             | 7              | 10             |
| 3                   | 7              | 12             | 8              |
| 4                   | 5              | 5              | 10             |
| 5-10                | 6              | 17             | 25             |
| 10-20               | 4              | 7              | 6              |
| Over 20             | 1              | 2              | 2              |
| Not applicable      | 14             | 9              | 1              |
| No response         | 42             | 33             | 25             |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 15**

*In five years time (July 2008), what do you estimate your company performance to be?*

Tables A.18, A.19 and A.20 provide details of the responses provided to this question. Of the 100 responses, 16 Incubatees did not provide any answer to this question, while some Incubatees only provided details for part of the question.

Table B.17

**INCUBATEE FORECAST OF ANNUAL REVENUE BY 2008**

|                              | Percentage |
|------------------------------|------------|
| \$0                          | 6          |
| \$1-\$100,000                | 1          |
| \$100,001 - \$500,000        | 3          |
| \$500,001 - \$1,000,000      | 1          |
| \$1,000,001 - \$5,000,000    | 26         |
| \$5,000,001 - \$10,000,000   | 22         |
| \$10,000,001 - \$20,000,000  | 9          |
| \$20,000,000 - \$50,000,000  | 9          |
| \$50,000,001 - \$100,000,000 | 3          |
| over \$100,000,000           | 4          |
| No Response                  | 16         |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.18

**INCUBATEE FORECAST OF VALUE OF ANNUAL EXPORTS BY 2008**

|                              | Percentage |
|------------------------------|------------|
| \$0                          | 4          |
| \$1-\$100,000                | 1          |
| \$100,001 - \$500,000        | 3          |
| \$500,001 - \$1,000,000      | 3          |
| \$1,000,001 - \$5,000,000    | 35         |
| \$5,000,001 - \$10,000,000   | 12         |
| \$10,000,001 - \$20,000,000  | 5          |
| \$20,000,000 - \$50,000,000  | 4          |
| \$50,000,001 - \$100,000,000 | 4          |
| over \$100,000,000           | 3          |
| No Response                  | 26         |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Table B.19

**INCUBATEE FORECAST OF NUMBER OF FTE EMPLOYEES BY 2008**

|             | Percentage |
|-------------|------------|
| 0           | 5          |
| 1 – 5       | 5          |
| 6 – 10      | 18         |
| 11 – 20     | 25         |
| 21 – 30     | 9          |
| 31 – 40     | 6          |
| 41 – 50     | 5          |
| 51 – 100    | 5          |
| over 100    | 3          |
| No response | 19         |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 16**

*Since commencing incubation, have you taken steps to protect intellectual property?*

Table A.21 provides details of the percentage of Incubatees who have taken steps to protect their intellectual property.

Table B.20

**INCUBATEES INTELLECTUAL PROPERTY PROTECTION**

| Have you taken steps to protect your IP? | Percentage |
|--|------------|
| Yes                                      | 68         |
| No                                       | 22         |
| No response                              | 10         |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Those Incubatees who indicated that they had taken steps to protect their intellectual property were asked to specify the type of protection action taken, and of the number of actions taken. Table A.22 shows the results of this question.

Table B.21

**INTELLECTUAL PROPERTY PROTECTION UNDERTAKEN BY INCUBATEES**

|                                  | Percentage of Incubatees undertaking activity | Number of IP protection activities |
|----------------------------------|---|------------------------------------|
| Patents lodged                   | 38  | 94                                 |
| Copyright claims                 | 19  | 553                                |
| Trademarks                       | 19  | 30                                 |
| Circuit layout protection claims | 1   | 2                                  |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Under ‘Other’ the following were identified by some incubatees:

- Provisional patents.
- Confidentiality agreements with potential partners and suppliers.
- Licensing agreements.

**Question 17**

*What is the value at 30 June 2003 of your company’s investments and assets?*

Table B.22

**VALUE OF INCUBATEE INVESTMENTS AND ASSETS (PERCENTAGE)**

|                           | Investments | Physical Assets | Other Assets | Total |
|---------------------------|-------------|-----------------|--------------|-------|
| \$0                       | 32          | 9               | 7            | 5     |
| \$1-\$10,000              | 0           | 14              | 3            | 1     |
| \$10,001 - \$20,000       | 1           | 12              | 5            | 2     |
| \$20,001 - \$30,000       | 2           | 6               | 2            | 4     |
| \$30,001 - \$40,000       | 0           | 2               | 1            | 0     |
| \$40,001 - \$50,000       | 0           | 8               | 2            | 2     |
| \$50,001 - \$100,000      | 1           | 7               | 2            | 7     |
| \$100,000 - \$500,000     | 3           | 12              | 17           | 20    |
| \$500,001 - \$1,000,000   | 5           | 0               | 5            | 9     |
| \$1,000,001 - \$2,000,000 | 1           | 2               | 7            | 9     |
| over \$2,000,001          | 1           | 0               | 4            | 7     |
| No response               | 54          | 28              | 45           | 34    |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 18**

(a) What are the success indicators you use for your company?

A significant range of responses were received for this question. Table A.24 shows the 15 most common responses to this question from the incubatees.

Table B.23

**TOP 15 SUCCESS INDICATORS FOR INCUBATEES**

|  | Percentage |
|--|------------|
| Sales                                    | 31         |
| Revenue                                  | 23         |
| Profit                                   | 15         |
| Customer satisfaction/feedback           | 10         |
| Number of clients                        | 10         |
| Product development                      | 9          |
| Market acceptance                        | 5          |
| Strategic partnerships                   | 5          |
| Reaching business milestones             | 5          |
| Return on investment                     | 4          |
| Cash flow                                | 3          |
| Intellectual property                    | 3          |
| Exports                                  | 2          |
| Staff satisfaction                       | 2          |
| Successful trials and territory launches | 2          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Other indicators provided by Incubatees included:

- ability to raise funding;
- ability to secure commercial agreements;
- achieving budgets;
- brand recognition;
- contract win;
- contribution to the community;
- establishment of reseller network;
- execution of contracts and agreements;
- market share;
- meeting customer requirements;
- number of service contracts;
- operational milestones;
- product awareness; and
- share price.

(b) To 30 June 2003, please explain the extent to which your company has progressed in line with your expectations?

Table B.24

**INCUBATEE PROGRESS AGAINST EXPECTATIONS**

|                           | Percentage |
|---------------------------|------------|
| Above expectations        | 11         |
| In-line with expectations | 37         |
| Below expectations        | 47         |
| No response               | 5          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

(c) What have been the most important influences on the progress of your company to date?

Table B.25

**TOP 15 INFLUENCES ON INCUBATEE PROGRESS**

|   | Percentage |
|---|------------|
| Availability of funds/capital             | 23         |
| BITS Incubator Program                    | 22         |
| Market conditions (positive and negative) | 19         |
| Insufficient capital                      | 13         |
| Strong networks                           | 13         |
| Product development                       | 11         |
| Experience of management                  | 7          |
| Motivation of founders                    | 7          |
| Staff skills                              | 6          |
| Contribution of board members             | 6          |
| Quality of investors                      | 5          |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 19**

Was a formal or structured business development training program offered to you as a service by your Incubator? If yes, did you accept the offer?

Table B.26

**BUSINESS DEVELOPMENT TRAINING**

| Were you offered a formal/structured business development training Program? | Percentage |
|---|------------|
| Yes   | 22         |
| No  | 73         |
| No response   | 5          |
| If yes, did you accept?   |            |
| Yes   | 57         |
| No  | 43         |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 20**

*What other kind of services have been provided either directly to you by your Incubator or arranged through other providers?*

Table B.27

**SERVICES OFFERED DIRECTLY AND INDIRECTLY TO INCUBATEES**

|                                     | In-House | External |
|-------------------------------------|----------|----------|
| Advice with business planning       | 68       | 17       |
| Financial management advice         | 47       | 22       |
| Legal or accounting services        | 27       | 40       |
| Mentoring program                   | 48       | 18       |
| Marketing and sales services        | 39       | 27       |
| Secretarial services                | 36       | 4        |
| Networking opportunities            | 66       | 29       |
| Provision of Incubatee board member | 53       | 5        |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Incubatees were also asked to rank the importance of the services. Table A.29 provides the aggregated importance ranking for each service. Not all incubatees ranked all services.

Table B.28

**IMPORTANCE OF SERVICES OFFERED TO INCUBATEES**

|                                     | Score | Importance Ranking |
|-------------------------------------|-------|--------------------|
| Advice with business planning       | 2.4   | 1                  |
| Financial management advice         | 3.4   | 2                  |
| Marketing and sales services        | 3.5   | 3                  |
| Networking opportunities            | 3.8   | 4                  |
| Mentoring program                   | 4.0   | 5                  |
| Legal or accounting services        | 4.5   | 6                  |
| Provision of Incubatee board member | 4.6   | 7                  |
| Secretarial services                | 6.6   | 8                  |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 21**

*What facilities were available to you in the Incubator?*

Table A.30 shows the proportion of Incubatees who responded to the survey who were provided with facilities.

Table B.29

**FACILITIES AVAILABLE TO INCUBATEES THROUGH THEIR INCUBATOR**

|                                | Percentage of Incubatees |
|--------------------------------|--------------------------|
| Physical Space                 | 53                       |
| Office Equipment (copier, fax) | 50                       |
| Server/LAN                     | 44                       |
| High Speed Internet access     | 47                       |
| Workshop                       | 23                       |
| Other                          | 17                       |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Under 'Other' the following were identified.

- Board rooms, rooms etc.
- Computing equipment.
- Web development.

**Question 22**

*Please describe any services or facilities that were not offered or provided that you think would have improved your incubation experience.*

Of the 100 Incubatees who responded to the survey, 38 provided a response to this question. Of these, five indicated that they were happy with the services that they had been provided. There was a wide range of suggestions provided, the most common being marketing services, with four Incubatees suggesting they would have liked to have been provided with more marketing services. Table A.34 provides

Table B.30

**ADDITIONAL SERVICES TO BE PROVIDED TO INCUBATEES**

|                          | Number of Incubatees |
|--------------------------|----------------------|
| Marketing services       | 4                    |
| Sales services           | 4                    |
| Legal services           | 2                    |
| Business Training        | 2                    |
| Accounting services      | 2                    |
| Recruitment              | 2                    |
| Networking opportunities | 2                    |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

Other suggestions included:

- workshop;
- better verifying of external service providers;
- more capital;
- early assessment of business strengths and weaknesses;
- formal financial advice;
- introductions to potential clients;
- secretarial services;
- reasonably priced accommodation;
- assistance with grant applications; and
- advice from successful business people.

**Question 23**

*How do you rate the performance of your Incubator at providing the following services and facilities?*

Incubatees were asked to rate the performance of the Incubator at providing 13 different services, and also rate the overall performance of the Incubator. Table A.32 provides details of the rating given by those Incubatees who responded to the survey.

Table B.31

**INCUBATEE RATING OF INCUBATOR PERFORMANCE, ALL INCUBATORS (PERCENTAGE)**

|                                       | Poor | Fair | Good | Very Good | Excellent | Not Applicable |
|---------------------------------------|------|------|------|-----------|-----------|----------------|
| Business development training program | 15   | 8    | 18   | 5         | 5         | 49             |
| Advice with business planning         | 6    | 12   | 29   | 29        | 11        | 13             |
| Financial management advice           | 7    | 11   | 14   | 25        | 12        | 31             |
| Legal or accounting services          | 11   | 15   | 19   | 12        | 4         | 39             |
| Mentoring program                     | 6    | 11   | 22   | 16        | 14        | 31             |
| Marketing and sales services          | 12   | 11   | 18   | 19        | 5         | 35             |
| Secretarial services                  | 6    | 13   | 11   | 7         | 11        | 52             |
| Networking opportunities              | 5    | 17   | 21   | 24        | 15        | 18             |
| Provision of Incubatee board member   | 10   | 6    | 14   | 15        | 22        | 33             |
| Physical Space                        | 3    | 5    | 15   | 14        | 17        | 46             |
| Office Equipment (copier, fax)        | 5    | 4    | 12   | 13        | 19        | 47             |
| Server/LAN                            | 6    | 4    | 13   | 13        | 14        | 50             |
| High Speed Internet access            | 8    | 4    | 11   | 15        | 14        | 48             |
| Workshop                              | 5    | 5    | 3    | 7         | 5         | 75             |
| Overall                               | 7    | 10   | 20   | 22        | 20        | 21             |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 24**

*In relation to **in-kind contributions** received from your Incubator, or through your Incubator, do you consider that these **represent value for money**? That is, do you think that you would have been unable to get a better deal spending the funds yourself?*

Table B.32

**VALUE FOR MONEY OF IN-KIND CONTRIBUTIONS**

| <b>Did the in-kind contributions received from your incubator represent value for money?</b>    | <b>Percentage</b> |
|---|-------------------|
| Yes   | 55                |
| No  | 17                |
| Not Applicable  | 15                |
| No response   | 13                |
| <b>Did the in-kind contributions received through your incubator represent value for money?</b> | <b>Percentage</b> |
| Yes   | 39                |
| No  | 13                |
| Not Applicable  | 15                |
| No response   | 33                |

Source: BITS Program Evaluation Survey for Incubatees – Survey results.

**Question 25**

*Please comment on the key **strengths and weaknesses** of your incubation experience to date.*

Responses provided remain commercial-in-confidence. Some responses are provided in the main body of this report.

*Appendix C*

**Questionnaires – Incubators and Incubatees**

Commonwealth Government Evaluation of the Building on  
Information Technology Strengths (BITS) Incubator Program  
*Evaluation Questionnaire for BITS Incubators*

Dear BITS Incubator

The BITS Incubator Program is currently being evaluated by The Allen Consulting Group, on behalf of the Commonwealth Department of Communication, Information Technology and the Arts (DCITA) to identify the key design features impacting on the success of the Program and other factors that might influence the design of future activities and the level of funding available.

Your participation in the evaluation is flagged in your Grant Deed Agreement with DCITA. We would be grateful if you could assist the evaluation by completing this short questionnaire in a timely fashion.

The questions are designed to help us to build a picture of the total performance of the BITS Incubator Program from commencement up until 30 June 2003 and may contribute to future planning of government sponsored incubation activities.

*If you would like to include additional information in your answers please do so on a separate sheet of paper and attach to the end of the questionnaire.*

The information collected through this Questionnaire process will feed into a document similar to the BITS Incubator Program Pilot Evaluation document.

We appreciate your cooperation, and trust that you will be able to assist by providing the information sought by **cob 18 July 2003**. If you have any questions or wish to clarify any issues, please contact either Dr John Bell or Mr John Burch on 02 6230 0185. If you consider that any of the information you provide is particularly sensitive please also bring this to the attention of Dr John Bell or Mr John Burch.

Please return your completed questionnaire by fax (using the enclosed Fax Back Cover Sheet) to The Allen Consulting Group on 02 6230 0149.

# Questionnaire

## General Information

1. Name of Incubator .....  
Contact person .....  
Telephone number .....  
Facsimile number .....  
Email address .....
2. What is the date on which your **Incubator commenced business**?  
Started in ..... (month) ..... (year).

## Financial Matters

**Questions 4, 5 and 6 below ask for information about the financial *inputs* to your Incubator. These are followed by questions 7, 8 and 9, which cover the investments or *outputs* from your Incubator.**

3. What are the **total BITS funds allocated** in your Grant Deed Agreement?  
\$.....
4. What is the total of BITS funds you have actually *received* from the Commonwealth to 30 June 2003, including interest earned on the grant funds?  
**Total BITS funding received**

---

|                                   |         |
|-----------------------------------|---------|
| (a) Total BITS funds (cash)       | \$..... |
| (b) Interest earned on BITS funds | \$..... |

---
5. What is the approximate *total* value of any in-kind contributions you have actually received to 30 June 2003? (please *tick one box from the selection below*). (In thinking about the value of in-kind contributions, please use *approximate* market values as a guide.) Under (b) and (c) in the table below, please also report the (approximate) percentage of total in-kind contributions provided to your Incubator and the percentage of total in-kind contributions provided to your Incubatees *through your Incubator* provided by other parties. **This question aims to collect information about in-kind contributions leveraged by the BITS Program.**

**Total value of in-kind contributions received**

---

|  |  |                          |            |                          |
|--|--|--------------------------|------------|--------------------------|
| (a) Total dollar value   | \$0-50K                                | <input type="checkbox"/> | \$50-100K  | <input type="checkbox"/> |
|  | \$100-150K                             | <input type="checkbox"/> | \$150-200K | <input type="checkbox"/> |
|  | \$200-250K                             | <input type="checkbox"/> | \$200-250K | <input type="checkbox"/> |
|  | \$250-300K                             | <input type="checkbox"/> | \$300-350K | <input type="checkbox"/> |
|  | \$350-400K                             | <input type="checkbox"/> | \$400-450K | <input type="checkbox"/> |
|  | \$450-500K                             | <input type="checkbox"/> |            |                          |
|  | Greater than \$500K – (please specify) |                          |            | \$.....                  |
| (b) Percentage provided to your Incubator                                |  |                          |            | .....%                   |
| (c) Percentage provided to your Incubatees <i>through your Incubator</i> |  |                          |            | .....%                   |

---

6. What is the total of other (that is, non BITS) funds that have actually been *received* by your Incubator for any purposes to 30 June 2003? **This question aims to collect information about other financial contributions leveraged by the BITS Program.**

**Total non BITS funding received**

---

|   |                |
|---|----------------|
| (a) Total funds <i>received</i> from Shareholders/guarantors  | \$.....        |
| (b) Total of own funds used   | \$.....        |
| (c) Total funds <i>received</i> from <i>State Government</i> sources<br>(please specify below)  | \$.....        |
| .....   |                |
| (d) Total funds <i>received</i> from other sources (please specify below)*  | \$.....        |
| .....   |                |
| (e) Total funds <i>received</i> from Incubatees for services provided ( <u>excluding</u><br>any of the BITS funding covered previously in <i>Question 4</i> ) | \$.....        |
| <b>(f) Total of (a)-(e) above</b>   | <b>\$.....</b> |

\*Including rent contributions paid to you.

---

7. What costs did you incur in setting up your Incubator? Please indicate the (approximate) percentage contribution that each type of cost makes to the total, and provide a total dollar cost.

**Incubator setting up costs\***

---

|                                     |                |
|-------------------------------------|----------------|
| (a) Preparation of legal documents  | .....%         |
| (b) Initial staff recruitment costs | .....%         |
| (c) Fit out costs                   | .....%         |
| (d) Networking infrastructure       | .....%         |
| (e) Office equipment                | .....%         |
| (f) Other setting up costs          | .....%         |
| <b>(g) Total dollar cost</b>        | <b>\$.....</b> |

\*Setting up costs are *initial* costs that are usually incurred in the first three months of a business, *excluding* those costs that are of an ongoing or running cost nature – see Q.8 below.

---

8. What are your Incubator running costs? These do not include investments in Incubatees or the value of services provided to Incubatees on a charge back basis (both are covered in Question 9). For each year below, please indicate the (approximate) percentage contribution that each type of cost makes to the total, and provide a total dollar cost.

**Incubator running costs**

|  | 2000-01        | 2001-02        | 2002-03        |
|--|----------------|----------------|----------------|
| (a) Total payroll/benefits                             | .....%         | .....%         | .....%         |
| (b) Building costs such as maintenance, mortgage/lease | .....%         | .....%         | .....%         |
| (c) Costs such as services to tenants                  | .....%         | .....%         | .....%         |
| (d) Other costs such as utilities, IT, supplies        | .....%         | .....%         | .....%         |
| (e) Other Incubator administration costs               | .....%         | .....%         | .....%         |
| (f) Other costs – such as networking functions         | .....%         | .....%         | .....%         |
| <b>(g) Total dollar cost</b>                           | <b>\$.....</b> | <b>\$.....</b> | <b>\$.....</b> |

9. What is the breakdown of your Incubator’s investments up to 30 June 2003? Please use the following investment categories, but exclude incubator setting up and running costs (which are covered in Q’s 7 and 8 above). **The total (g) should be equal to the totals for Q’s 4, 5 and 6, minus the totals for Q’s 7 and 8 (for 2000-01 to 2002-03).**

**Incubator investments**

|   |                |
|---|----------------|
| (a) Funds actually <i>given</i> to Incubatees (cash)  | \$.....        |
| (b) The value of in-kind and other services provided to Incubatees on a charge back basis to the Incubator* | \$.....        |
| (c) BITS funds notionally <i>allocated</i> to Incubatees but not yet invested                               | \$.....        |
| (d) Other investment items  | \$.....        |
| (e) Cash on hand  | \$.....        |
| (f) Other assets valued at cost#  | \$.....        |
| <b>(g) Total</b>  | <b>\$.....</b> |

\*These are services that have been allocated to Incubatees but are drawn down as the Incubator provides services on a charge back basis. This includes advice, rent etc.

#Acquired since the Incubator began, but not including setting up costs.

10. What costs have you incurred up to 30 June 2003 in meeting *reporting and other DCITA requirements*. These costs will form part of the running costs that you described in Question 8, but will probably overlap the categories used in that Question. (It is understood that it is difficult to calculate compliance costs with a great degree of precision, so please provide your best estimate.) Please also provide the total costs you incurred in your *initial application for BITS funding* from DCITA.

**Compliance costs**

|  |                |
|--|----------------|
| (a) Costs in meeting reporting and other DCITA requirement | \$.....        |
| (b) Costs in you initial application for BITS funding      | \$.....        |
| <b>(c) Total costs</b>                                     | <b>\$.....</b> |

11. What is the estimated total amount of additional investment (including business angel, venture capital and other investors) that has been received by your **Incubatees** to 30 June 2003 that you feel your Incubator has had a facilitating role in?

**Additional investment**

---

|  |                |
|--|----------------|
| (a) From Business Angels                       | \$.....        |
| (b) From Venture Capitalists                   | \$.....        |
| (c) From other Commonwealth Government sources | \$.....        |
| (d) From other State Government sources        | \$.....        |
| (e) From other sources                         | \$.....        |
| <b>(f) Total</b>                               | <b>\$.....</b> |

---

12. As flagged in your BITS Grant Deed, have you developed a close **relationship with an investments fund**?

Yes  (go to Question 13) No

If not, why not? (tick one box)

Found it easier/more practical to shop around on a case-by-case basis

Was unable to find an investment fund interested in being involved

Other reason (please describe below)

.....  
 .....  
 .....  
 .....

13. BITS funding is scheduled to cease on 30 June 2004. Looking forward, how do you assess the prospects of your Incubator after that time? (please tick relevant boxes)

**Incubator prospects**

---

(a) Incubator activities could be maintained at current levels

(b) Incubator activities would need to be reduced significantly

(c) Incubator would need further funding

(d) Incubator would take at least 12 months to be viable

(e) Incubator would take more than 12 months to be viable

(f) Other impacts on Incubator activities (please specify)

.....  
 .....  
 .....

---

14. What is the value\* at 30 June 2003 of Incubator investments and assets ?

**Incubator investments and assets**

|   |                |
|---|----------------|
| (a) Incubatee investments               | \$.....        |
| (b) Other investments                   | \$.....        |
| (c) Physical assets                     | \$.....        |
| (d) Other assets                        | \$.....        |
| <b>(e) Total investments and assets</b> | <b>\$.....</b> |

\*Please include (on the Fax Back Cover Sheet) the basis on which these investments have been valued.

**Business Model Characteristics**

15. Please indicate your type of Incubator (*tick one box*)

**Type of Incubator**

|              |                          |
|--------------|--------------------------|
| (a) Virtual  | <input type="checkbox"/> |
| (b) Physical | <input type="checkbox"/> |
| (c) Mixed*   | <input type="checkbox"/> |

\*Mixed is physical and virtual

16. Please indicate the rate and amount of equity you take in respect of your Incubatees.

**Rate and amount of equity**

|  |         |
|--|---------|
| (a) Highest rate of equity you have taken              | .....%  |
| (b) Lowest rate of equity you have taken               | .....%  |
| (c) Average rate of equity you usually take            | .....%  |
| (d) Total value of original equity taken in Incubatees | \$..... |
| (e) Less equity written off value at 30 June 2003      | \$..... |

17. How many **Incubator staff** do you have – as at 30 June 2003? ..... FTE\*

\* Full Time Equivalent (FTE) expresses part time staff as a proportion of a full time position. Someone working two days a week is 0.4 FTE, for example.

18. What was the average FTE staff of your Incubator in each of the years of operation? You may estimate these figures if you do not have exact data.

**Incubator staff**

|                             | <u>2000-01</u> | <u>2001-02</u> | <u>2002-03</u> |
|-----------------------------|----------------|----------------|----------------|
| Average FTE Incubator staff | .....          | .....          | .....          |

19. In working with your Incubatees:

Please indicate the investment model\* you use. *(tick the boxes that apply)*

**Investment model**

---

- (a) Cash only *(go to question 20)*
- (b) Services only *(go to question 20)*
- (c) Blend

If a blend, what is the proportion of cash and services that you provide?

Cash proportion .....%

Services proportion .....%

\*Investment models - **Cash only** – that is, seed funding is provided to Incubatees who in some cases may buy back services from the Incubator. **Services only** –no cash is provided. **Blend** – you provide a mix of cash and services.

---

20. Please indicate your business structure *(tick one box)*

**Incubator business structure**

---

- (a) Not-for-profit
- (b) Profit
- (c) Books model (balancing costs against profits)
- (d) Other *(please explain)*

.....

.....

.....

.....

---

21. Do you offer a business development training program as a service to your Incubatees?

Yes  No  *(please go to question 22)*

If yes, please indicate the nature of your training program? *(tick all that apply)*

**Training program**

---

- (a) Structured business development training program conducted in-house
- (b) Structured business development training program outsourced
- (c) Occasional sessions conducted in-house
- (d) Occasional session outsourced
- (e) Other *(please describe)* .....

.....

---

22. What other kind of services have been provided either directly by the Incubator or arranged through other providers? (*tick all that apply*) Please also rank your view of the importance of each of these other services *relative to each other* in terms of how they contribute to a successful incubation experience for Incubatees.

**Other services provided by Incubators**

|   | Provided                 |                          | Importance |
|---|--------------------------|--------------------------|------------|
|   | In-House                 | Externally               | Ranking*   |
| (a) Advice with business planning       | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (b) Financial management advice         | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (c) Legal or accounting services        | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (d) A Mentoring program                 | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (e) Marketing and sales services        | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (f) Secretarial services                | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (g) Networking opportunities            | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (h) Use of meeting rooms                | <input type="checkbox"/> | <input type="checkbox"/> | .....      |
| (i) Provision of Incubatee board member | <input type="checkbox"/> | <input type="checkbox"/> | .....      |

\*Please rank the importance of each of these other services *relative to each other* on a 1-9 scale, with 1 being the most important and 9 being the least important.

23. If you offer physical incubation facilities:  
 how much space do you have available for Incubatees? .....sq m  
 what is the average space allocated per Incubatee? ..... sq m  
 which of the following facilities do you provide? (*tick all that apply*)

**Incubation facilities**

- |   |                          |
|---|--------------------------|
| (a) Office services (eg receptionist, typing) | <input type="checkbox"/> |
| (b) Office equipment (Photocopier, fax)       | <input type="checkbox"/> |
| (c) Server/LAN                                | <input type="checkbox"/> |
| (d) High speed Internet access                | <input type="checkbox"/> |
| (e) Workshop                                  | <input type="checkbox"/> |
| (f) Other ( <i>please specify</i> )           | <input type="checkbox"/> |

.....

24. What triggers graduation\* for your Incubatees? (*tick one box*)

**Graduation triggers**

- (a) Completion of a structured business development training program
- (b) End of Incubator agreement
- (c) Other performance indicators, criteria or milestones   
(*please describe*)

.....  
 .....

\*Graduation occurs when a Program participant reaches a stage when:

- their period of support in the Incubator is over
- they meet their Incubator’s graduation criteria
- they are developed sufficiently to move to a more independent setting

**Client Information**

25. Please provide information about the throughput of your Incubator.

**Incubator throughput statistics**

|  | <u>2000-01</u> | <u>2001-02</u> | <u>2002-03</u> |
|--|----------------|----------------|----------------|
| (a) Total applicants                                       | .....          | .....          | .....          |
| (b) Total Incubatees accepted                              | .....          | .....          | .....          |
| (c) No. Incubatees in (2) receiving <\$50,000 <sup>1</sup> | .....          | .....          | .....          |
| (d) No. Incubatees in (2) receiving >\$50,000 <sup>1</sup> | .....          | .....          | .....          |
| (e) No. Graduates from (c) <sup>2</sup>                    | .....          | .....          | .....          |
| (f) No. Graduates from (d) <sup>2</sup>                    | .....          | .....          | .....          |
| (g) No. Incubatees that are withdrawals <sup>3</sup>       | .....          | .....          | .....          |
| (h) No. of Graduates from (c) still trading <sup>2,4</sup> | .....          | .....          | .....          |
| (i) No. of Graduates from (d) still trading <sup>2</sup>   | .....          | .....          | .....          |

<sup>1</sup>Including cash and in-kind investments

<sup>2</sup>Please insert Graduates into the year that they graduated

<sup>3</sup>Please insert these into the year that they last received incubation assistance

<sup>4</sup>Only provide information on these if it is readily available to you

26. What is the average time that an Incubatee spends in your Incubator before Graduating? Please distinguish between Incubatees receiving <\$50,000 and those receiving >\$50,000.

**Average Incubatee stay**

|   |              |
|---|--------------|
| Average Incubatees stay for those receiving <\$50,000 | ..... months |
| Average Incubatees stay for those receiving >\$50,000 | ..... months |

27. Please indicate the various sources of your Incubatees. *(tick all that apply)*

**Source of Incubatees**

|   |                          | % of Incubatees |
|---|--------------------------|-----------------|
| (a) From Universities, government labs and CRCs | <input type="checkbox"/> | .....%          |
| (b) ICT industry contact or network             | <input type="checkbox"/> | .....%          |
| (c) Other industry contact or network           | <input type="checkbox"/> | .....%          |
| (d) Other                                       | <input type="checkbox"/> | .....%          |

**Financial and Other Outcomes**

28. What is the total number and value of **Investment Exits** your Incubator has achieved?

Total number .....  
 Total value \$.....

29. In relation to your Incubator’s Incubatees and Graduates, what **commercial outcomes** have you been able to achieve?

**Commercial outcomes**

|   |                 |                |
|---|-----------------|----------------|
| (a) Number of trade sales                         | Australia ..... | Offshore ..... |
| (b) Value of trade sales                          | \$.....         | \$.....        |
| (c) Number of floats                              | Australia ..... | Offshore ..... |
| (d) Value of floats                               | \$.....         | \$.....        |
| (e) Number Graduate share sales                   | Australia ..... | Offshore ..... |
| (f) Value of Graduate share sales                 | \$.....         | \$.....        |
| (g) Number of write offs                          |                 | .....          |
| (h) Other outcomes <i>(please describe below)</i> | .....           |                |
|   | .....           |                |

30. What are the employment, total revenue and export revenue outcomes that have been achieved by your Incubatees and Graduates (if you have this information) since they began their incubation up to 30 June 2003? Please exclude withdrawals from these totals.

**Incubatee outcomes**

|                      |                                |                         |
|----------------------|--------------------------------|-------------------------|
| (a) Employment (FTE) | at start of incubation .....   | at 30 June 2003 .....   |
| (b) Total revenue    | at start of incubation \$..... | at 30 June 2003 \$..... |
| (c) Export revenue   | at start of incubation \$..... | at 30 June 2003 \$..... |

31. Please comment on the key **strengths and weaknesses** of your Incubator operation to date?

.....  
.....  
.....  
.....  
.....

32. Are there any **particular characteristics of the region** you are physically located in that you feel impact on:

- aspects of your Incubator’s operation, such as proximity of complementary businesses or services;
- the kind, quality and quantity of Incubatee applications you receive; and
- the outcomes you have achieved.

.....  
.....  
.....  
.....

33. Please comment on the nature of **support that you have been able to get from the business community** in relation to your Incubator. For instance, describe the nature of any services you have been able to secure from your local business community at discounted rates or on a volunteer basis.

.....  
.....  
.....  
.....

34. **How long** did it take you to:

- (a) prepare for this Questionnaire ..... minutes  
(b) actually complete the Questionnaire ..... minutes

Thank you for completing this Evaluation Questionnaire. Please send the completed Questionnaire to Dr John Bell by fax (using the enclosed Fax Back Form) by **cob 18 July 2003**.

Dr John Bell

Associate Director  
The Allen Consulting Group  
GPO Box 418  
Canberra ACT 2600

Fax: 02 6230 0149  
Phone: 02 6230 0185  
Email: [jbell@allenconsult.com.au](mailto:jbell@allenconsult.com.au) cc. [jburch@allenconsult.com.au](mailto:jburch@allenconsult.com.au)

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**Commercial-In-Confidence when completed**

**Commonwealth Government Evaluation of the Building on  
Information Technology Strengths (BITS) Incubator Program  
Evaluation *Questionnaire for BITS Incubatees & Graduates***

Dear BITS Incubatee/Graduate

The BITS Incubator Program is currently being evaluated by The Allen Consulting Group, on behalf of the Commonwealth Department of Communication, Information Technology and the Arts (DCITA) to identify the key design features impacting on the success of the Program and other factors that might influence the design of future activities and the level of funding available.

The Incubators and the DCITA would be grateful if you could assist the evaluation by completing this short questionnaire.

The questions are designed to help us to build a picture of the total performance of the BITS Incubator Program from commencement up until 30 June 2003 and may contribute to future planning of government sponsored incubation activities.

If you would like to include additional information in your answers please do so on a separate sheet of paper and attach to the end of the questionnaire.

Some Incubatees were involved in a Pilot Evaluation of the BITS Incubator Program in late 2002. The Pilot Evaluation report can be viewed at:

[www.dcita.gov.au/Article/0,,0\\_1-2\\_11-3\\_463-4\\_113634,00.html](http://www.dcita.gov.au/Article/0,,0_1-2_11-3_463-4_113634,00.html)

This current evaluation covers all the BITS Incubators, Incubatees and Graduates, and seeks different information to that sought in late 2002.

We appreciate your cooperation, and trust that you will be able to assist by providing the information sought by **cob 25 July 2003**. If you have any questions or wish to clarify any issues, please contact either Dr John Bell or Mr John Burch on 02 6230 0185. If you consider that any of the information you provide is particularly sensitive please also bring this to our attention.

Please return your completed questionnaire by fax (using the enclosed Fax Back Form) to The Allen Consulting Group on 02 6230 0149.

Please be assured that all information collected will be treated as **Commercial-In-Confidence**.

Questionnaire

General Information

- 1. Name of Incubatee/Graduate .....
- Contact person .....
- Telephone number .....
- Facsimile number .....
- Email address .....

The name of your Incubator is .....

- 2. On what date did your Incubation commence?  
Started in ..... (month) ..... (year).

- 3. If you have graduated from incubation, what was your date of graduation?  
..... (month) ..... (year).

- 4. If you are a 'withdrawal' from an Incubator, please indicate the reason for your withdrawal.

Reasons for 'withdrawal'

- (a) Lack of commercial prospects
- (b) Disagreement with Incubator management
- (c) Inadequate funding
- (d) Market for product/service not ready
- (e) Other (please specify)

.....  
.....  
.....  
.....  
.....

(If you answer Question 4, you may not be in a position to answer all of the following questions – if this is the case, please respond only to the questions you feel you can answer easily)

**Commercial-In-Confidence when completed**

**Financial Matters**

5. What is the total of BITS funds (cash) you have actually received from your Incubator up to 30 June 2003?

**BITS funding received from Incubator**

Total BITS funds (cash) \$.....

6. What is the total of BITS funds (cash) you have yet to receive from your Incubator (possibly subject to milestones)?

**BITS funding yet to be received from Incubator**

Total BITS funds (cash) \$.....

7. What is the approximate *total* value of any in-kind contributions provided by or through your Incubator that you have actually received to 30 June 2003? (please *tick one box from the selection below*). In-kind contributions include goods and/or services paid for by your Incubator such as computer equipment or services – Question 20 provides a list of the sorts of in-kind services provided. (In thinking about the value of in-kind contributions, please use *approximate* market values as a guide.) **This question aims to collect information about in-kind contributions leveraged by the BITS Program.** (see next page).

**Total value of in-kind contributions received from your Incubator**

|                    |  |                          |            |                          |
|--------------------|--|--------------------------|------------|--------------------------|
| Total dollar value | \$0-50K                                | <input type="checkbox"/> | \$50-100K  | <input type="checkbox"/> |
|                    | \$100-150K                             | <input type="checkbox"/> | \$150-200K | <input type="checkbox"/> |
|                    | \$200-250K                             | <input type="checkbox"/> | \$200-250K | <input type="checkbox"/> |
|                    | \$250-300K                             | <input type="checkbox"/> | \$300-350K | <input type="checkbox"/> |
|                    | \$350-400K                             | <input type="checkbox"/> | \$400-450K | <input type="checkbox"/> |
|                    | \$450-500K                             | <input type="checkbox"/> |            |                          |
|                    | Greater than \$500K – (please specify) |                          |            | \$.....                  |

8. What is the approximate total value of any in-kind contributions you have actually received to 30 June 2003 *from sources other than your incubator*? (please tick one box from the selection below).

**Total value of in-kind contributions received from elsewhere**

|                    |  |                          |            |                          |
|--------------------|--|--------------------------|------------|--------------------------|
| Total dollar value | \$0-50K                                | <input type="checkbox"/> | \$50-100K  | <input type="checkbox"/> |
|                    | \$100-150K                             | <input type="checkbox"/> | \$150-200K | <input type="checkbox"/> |
|                    | \$200-250K                             | <input type="checkbox"/> | \$200-250K | <input type="checkbox"/> |
|                    | \$250-300K                             | <input type="checkbox"/> | \$300-350K | <input type="checkbox"/> |
|                    | \$350-400K                             | <input type="checkbox"/> | \$400-450K | <input type="checkbox"/> |
|                    | \$450-500K                             | <input type="checkbox"/> |            |                          |
|                    | Greater than \$500K – (please specify) |                          |            | \$.....                  |

**Commercial-In-Confidence when completed**

9. What is the total of other (that is, non BITS) funds that you have actually *received* for any purposes to 30 June 2003? **This question aims to collect information about other financial contributions leveraged by the BITS Program.**

**Total non BITS funding received**

|  | <b>Loans</b> | <b>Grants</b> | <b>Equity</b> |
|--|--------------|---------------|---------------|
| (a) Total non-BITS funds from your Incubator (if known)  | \$.....      | \$.....       | \$.....       |
| (b) Total funds received from Shareholders/guarantors  | \$.....      | \$.....       | \$.....       |
| (c) Total of own funds used  | \$.....      | \$.....       | \$.....       |
| (d) Total funds received from <i>Commonwealth Government</i> sources (please specify below)    |              |               |               |
| .....  | \$.....      | \$.....       | \$.....       |
| (e) Total funds received from <i>State/Territory Government</i> sources (please specify below) |              |               |               |
| .....  | \$.....      | \$.....       | \$.....       |
| (f) Funds received from other sources (specify below)  |              |               |               |
| .....  | \$.....      | \$.....       | \$.....       |
| <b>(g) Total of (a) to (f) above</b>   |              |               |               |

10. What is the ownership of your current equity?

**Current equity**

|                            |        |
|----------------------------|--------|
| (a) Yourself               | .....% |
| (b) Your Incubator         | .....% |
| (b) Business angels        | .....% |
| (c) Venture capitalists    | .....% |
| (d) Family and friends     | .....% |
| (e) Other (please specify) | .....% |
| .....                      |        |

11. **Does your Incubator hold options** in your company?

Yes                       No  (Go to Question 11)

If yes, please provide details of:

- the number of options. ....
- timing of the exercise of these options. ....
- the exercise price. \$.....

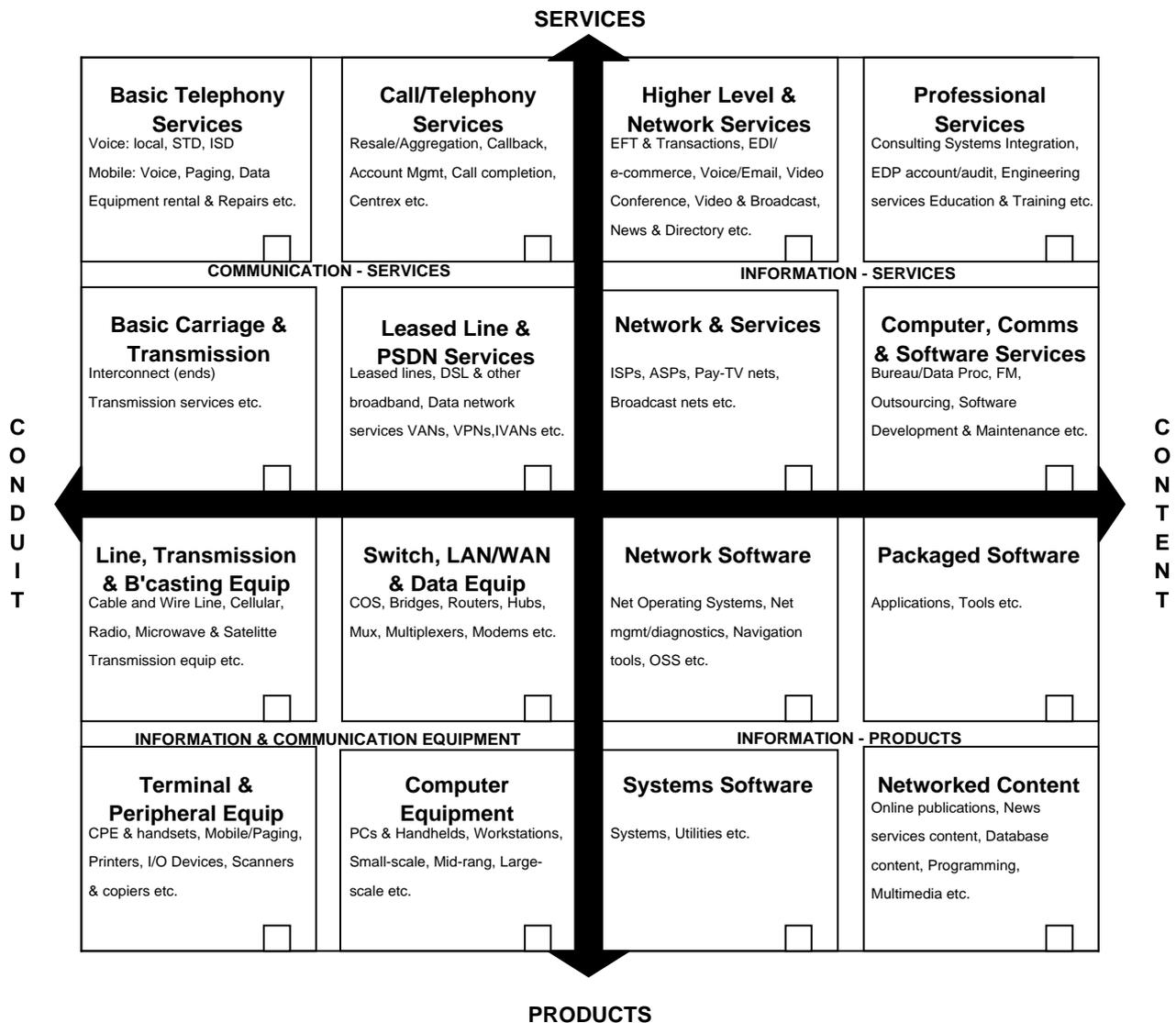
**Commercial-In-Confidence when completed**

**Business Characteristics**

12. What are the **major products/services** which your company provides?

- .....
- .....
- .....

13. How would you classify your company? Please tick the relevant box in the Information and Communications Technology Map overleaf.\*



Source: Productivity Commission, 1996, *Mapping The Information Industries*, Canberra.

**Commercial-In-Confidence when completed**

**Your Company's Progress**

14. Please provide the information requested below relating to your company's progress. Write "est" after figure which you have estimated, "p" after any number that represents only part of a year and "NA" for not applicable.

**Output statistics**

|                       | <b>2000-01</b> | <b>2001-02</b> | <b>2002-03</b> |
|-----------------------|----------------|----------------|----------------|
| (a) Revenue           | \$.....        | \$.....        | \$.....        |
| (b) Exports           | \$.....        | \$.....        | \$.....        |
| (c) Profit (if any)   | \$.....        | \$.....        | \$.....        |
| (d) Employment (FTE)* | .....          | .....          | .....          |

\* Full Time Equivalent (FTE) expresses part time staff as a proportion of a full time position. Someone working two days a week is 0.4 FTE, for example.

15. In five years time (July 2008), what do you estimate your company performance to be?

**Estimate of your company's performance in five years**

|                           |         |
|---------------------------|---------|
| Annual Revenue            | \$..... |
| Annual Value of exports   | \$..... |
| Number of employees (FTE) | .....   |

16. Since commencing incubation, have you taken steps to **protect intellectual property**?

Yes                       No  (*Go to Question 17*)

- (a) Number of patent applications lodged .....  
 (b) Number of copyright claims .....  
 (c) Number of circuit layout protection claims .....  
 (d) Other (please describe) .....  
 .....  
 .....  
 .....  
 .....

**Commercial-In-Confidence when completed**

17. What is the value\* at 30 June 2003 of your company's investments and assets?

**Company investments and assets**

---

- |   |                |
|---|----------------|
| (a) Investments                         | \$.....        |
| (b) Physical assets                     | \$.....        |
| (c) Other assets                        | \$.....        |
| <b>(d) Total investments and assets</b> | <b>\$.....</b> |

\*Please include (on the Fax Back Cover Sheet) the basis on which these investments have been valued.

---

18. (a) What are the **success indicators** you use for your company?

.....

.....

.....

.....

(b) To 30 June 2003, please explain **the extent to which your company has progressed in line with your expectations?**

.....

.....

.....

.....

(c) What have been the most important influences on the progress of your company to date?

1.....

2.....

3.....

4.....

Comment: .....

.....

|                                   |
|-----------------------------------|
| <b>Your Incubation Experience</b> |
|-----------------------------------|

19. Was a formal or structured **business development training program** offered to you as a service by your Incubator?

Yes                       No  (please go to question 20)

If yes, did you accept the offer?

Yes                       No

**Commercial-In-Confidence when completed**

20. What other kind of services have been provided either directly to you by your Incubator or arranged through other providers? (*tick all that apply*) Please also rank your view of the importance of each of these other services *relative to each other* in terms of how they should contribute to a successful incubation experience for Incubatees. That is, if you only actually received two of the other services listed below but have a view regarding the importance of other services, please rank these.

**Other services provided by Incubators**

---

|   | Provided                 |                          | Importance<br>Ranking* |
|---|--------------------------|--------------------------|------------------------|
|   | In-House                 | Externally               |                        |
| (a) Advice with business planning       | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (b) Financial management advice         | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (c) Legal or accounting services        | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (d) Mentoring program                   | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (e) Marketing and sales services        | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (f) Secretarial services                | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (g) Networking opportunities            | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |
| (h) Provision of Incubatee board member | <input type="checkbox"/> | <input type="checkbox"/> | .....                  |

\*Please rank the importance of each of these other services *relative to each other* on a 1-9 scale, with 1 being the most important and 9 being the least important.

---

21. What facilities were available to you in the Incubator? (*tick all that apply*)

**Incubation facilities**

---

- |                                     |                          |
|-------------------------------------|--------------------------|
| (a) Physical space                  | <input type="checkbox"/> |
| (b) Office equipment (copier, fax)  | <input type="checkbox"/> |
| (c) Server/LAN                      | <input type="checkbox"/> |
| (d) High speed Internet access      | <input type="checkbox"/> |
| (e) Workshop                        | <input type="checkbox"/> |
| (f) Other ( <i>please specify</i> ) | <input type="checkbox"/> |

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22. Please describe any services or facilities that were not offered or provided that you think would have improved your incubation experience?

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**Commercial-In-Confidence when completed**

23. How do you rate the performance of your Incubator at providing the following services and facilities? *(please tick one box for each row that is relevant to you)*

**Incubator performance at providing services and facilities**

|                                     | Poor                     | Fair                     | Good                     | Very Good                | Excellent                |
|-------------------------------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|
| (a) Business devt' training program | <input type="checkbox"/> |
| (b) Advice with business planning   | <input type="checkbox"/> |
| (c) Financial management advice     | <input type="checkbox"/> |
| (d) Legal or accounting services    | <input type="checkbox"/> |
| (e) Mentoring program               | <input type="checkbox"/> |
| (f) Marketing and sales services    | <input type="checkbox"/> |
| (g) Secretarial services            | <input type="checkbox"/> |
| (h) Networking opportunities        | <input type="checkbox"/> |
| (i) Provision of board member       | <input type="checkbox"/> |
| (j) Physical space                  | <input type="checkbox"/> |
| (k) Office equipment (copier, fax)  | <input type="checkbox"/> |
| (l) Server/LAN                      | <input type="checkbox"/> |
| (m) High speed Internet access      | <input type="checkbox"/> |
| (n) Workshop                        | <input type="checkbox"/> |
| <b>(o) Overall</b>                  | <input type="checkbox"/> |

24. In relation to **in-kind contributions** received from your Incubator, or *through* your Incubator, do you consider that these **represent value for money**? That is, do you think that you would have been unable to get a better deal spending the funds yourself?

(a) In-kind contributions from your Incubator:

Yes                       No

If no, please explain why not .....

.....

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.....

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(b) In-kind contributions received through your Incubator:

Yes                       No

If no, please explain why not .....

.....

**Commercial-In-Confidence when completed**

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25. Please comment on the key **strengths and weaknesses** of your incubation experience to date

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26. How long did it take you to:

- (a) prepare for this questionnaire ..... minutes
- (b) actually complete the questionnaire ..... minutes

Thank you for completing this Evaluation Questionnaire. Please send the completed Questionnaire to Dr John Bell by fax (using the enclosed Fax Back Cover Sheet) by **cob 25 July 2003**.

Dr John Bell  
Associate Director  
The Allen Consulting Group  
GPO Box 418  
Canberra ACT 2600

Fax: 02 6230 0149  
Phone: 02 6230 0185  
Email: [jbell@allenconsult.com.au](mailto:jbell@allenconsult.com.au) cc.  
[jburch@allenconsult.com.au](mailto:jburch@allenconsult.com.au)

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