

Creating Jobs Over Coffee

A new business incubator model could help build jobs in your city.

By *Kristen Carney*

Amid the grassy plains of Greensburg, Kansas, Scott and Susan Reinecke recently opened Studio 54 Glass, a glass art studio. Some 650 miles south, in Austin, Texas, Tina Cannon and Christy Scovel are bringing their Internet start-up, PetsMD.com, to life. These two businesses provide vastly different products, but they are alike in that business incubator programs have helped them grow.

The Greensburg Business Incubator, which leases space to Studio 54 Glass, is a traditional incubator — leasing space and providing business services for start-up firms — but the Capital Factory incubator, which is helping PetsMD, is something else entirely.

Two business incubator models

A tornado destroyed downtown Greensburg in May 2007. After surveys and public meetings identified the area's needs, the city secured \$3 million from the U.S. Department of Agriculture and Frito-Lay to build a facility that would encourage downtown growth. To accomplish this goal, the city built a 10,000-square-foot, LEED platinum business incubator with enough office space for 10 businesses. Studio 54 Glass was the first tenant there.

The Reineckes' retirement dream was to open a glass art studio, and the new incubator was just the opportunity that they needed. Studio 54 Glass pays about \$365 per month for its 800-square-foot retail space. "We wouldn't be able to do this without the business incubator," Scott Reinecke says, "because it's the only place in town for this business to have a go at it."

Businesses in the Greensburg Business Incubator have access to courses from the Kansas Small Business Development Center. The incubator is now completely full less than a year after it opened and is close to accomplishing its mission of serving as an anchor building and assisting in a revival of the downtown area.

Location, location, location? Not always.

Unlike Studio 54 Glass, online businesses like PetsMD don't require the perfect location in a downtown anchor building. PetsMD.com is an online encyclopedia of veterinarian-approved pet health information, where people can find vets and book appointments. Businesses like PetsMD can be run from coffee shops or spare bedrooms. Inexpensive space and business classes weren't what Tina Cannon, cofounder of PetsMD, needed to help her business grow. She needed mentors.

"For us, Capital Factory was a perfect fit," Cannon says. "We gained a tremendous amount of knowledge and rapid growth from the advice of our mentors. We were able to grow our company in 10 weeks, where in the regular business cycle it would have taken us up to a year to get here."

Capital Factory is a 10-week program that provides five start-ups with weekly mentoring sessions from a group of 20 experienced mentors who have founded successful companies. The incubator also provides a small amount of start-up capital along with the services of an attorney, a publicist, an accountant, and others. The five companies in the Capital Factory program currently employ 20 people, seven of whom work for PetsMD.

Another central difference between the mentor-model incubator and the traditional model is that the city of Austin paid nothing for Capital Factory. The program is privately funded by the mentors in exchange for a small ownership stake. Participating companies sell five percent of their businesses to Capital Factory in exchange for mentorship, start-up cash, and services. And all of the Capital Factory businesses are required to be located in Austin, because the mentors are located there.

Of all of the mentor-model incubator programs, the most famous is the Y Combinator seed-funding program started by Paul Graham. Graham started Viaweb in 1995 and sold it to Yahoo three years later for an estimated \$49 million, according to articles published at the time. While speaking to a group of college students interested in entrepreneurship, Graham advised them to raise money from investor-mentors with experience starting companies. After reflecting on his own advice, Graham started Y Combinator as an experiment in the summer of 2005.

Y Combinator paid each start-up founder \$6,000 in exchange for about six percent of the company. The founders were required to move to Cambridge, Massachusetts, where they would work out of their apartments, meet with Graham during office hours, and attend weekly seminars. More than 200 companies applied in the first year, and Graham funded eight of them. By the end of the first three-month program, he knew that his mentor-model program had merit. Y Combinator has funded 145 companies in both Cambridge and Mountain View, California, since 2005. The Y Combinator companies have created about 500 jobs — a number that will undoubtedly grow along with their companies.

Remarkably, the \$6,000 per start-up provided by Y Combinator doesn't add up to a lot of money. In fact, it typically won't even cover the start-up attorney's fees. However, \$6,000 will cover the living expenses of the founders, who share an apartment and dine on Ramen noodles for three months as they build their companies. Graham's business philosophy of building lean companies focused on solving problems, plus the rise of computers and the Internet, has made the mentor-model incubator possible.

Paul Graham is not the only businessman who has run a successful mentor-model incubator. Marc Nathan, a Capital Factory mentor and the director of entrepreneur development for the Houston Technology Center, estimates that 34 mentor-model incubators have been implemented worldwide in cities as diverse as Lexington, Kentucky; Athens, Greece; and Vancouver, Canada.

Despite the economic downturn, mentor-model incubators are seeing an increase in their number of applicants. Graham is expecting more than 1,000 companies to apply to Y Combinator's next session, five times the number of companies that applied in 2005. Capital Factory had over 250 companies apply for its first summer 2009 program, well above the 100 applicants that it expected.

Get rich quick or over the long haul?

Mentor-model incubators typically do not target a specific number of businesses or jobs. Rather, their goal is long-term profit.

Therefore, the only apparent shortcoming of this kind of incubator is that it seems like a get-rich scheme for wealthy investors — not a tool for planners to create jobs. Undoubtedly, these incubators are an investment opportunity, but there are many other motives for the investor-mentors.

Each of the 20 Capital Factory mentors owns 0.25 percent of each company. If one of the companies beats the lottery-sized odds and sells for \$10 million, each mentor would make \$25,000 — not exactly a big windfall for people who have already bought and sold successful businesses.

By owning a tiny slice of each company, the mentors are further motivated to help those companies succeed. Leveraging private dollars for public gain is not unheard of in the planning field. Public-private partnerships have long been helpful tools in the planner's tool belt. Private funding is a vital part of the mentor model, and innovative planners with a touch of their own entrepreneurial spirit could take steps to encourage mentor-model incubators in their backyards.

Which model is best for your city?

Gary Smith, who works in the Kansas office of the USDA, helped plan the Greensburg Business Incubator. Smith says the first step for planners is to ask, "What does the community have that they want to build upon?" In the case of Greensburg, it was the community's shared vision of rebuilding after its disastrous tornado. A traditional business incubator serving as a downtown anchor fit that vision. Additionally, the city was eligible for disaster funding to finance the incubator.

Consider your city's primary economic base and how you can build upon that base. If your current base includes location-needy sectors like retail and manufacturing, a traditional business incubator might be a better fit. But if your current base includes businesses that don't require a physical space, like technology and services, the mentor model might be preferable.

On the other hand, local economies can change. If your region's largest economic sector is agriculture, a mentor-model incubator might focus on teaching smaller farms how to make money from selling organic produce at local farmers markets. If your region is industrial, you might learn from the experience in Youngstown, Ohio — a classic Rust Belt city — where the Youngstown Business Incubator has received nationwide media attention for generating 300 technology jobs. But in the end, the type of incubator model for your city might come down to funding.

What to look for

With the mentor-model incubator, there are no funding forms to fill out or any grant paperwork to complete. Instead, you need to recruit a group of business-savvy men and women to serve as mentors. Recruiting the right people is undoubtedly the most important step. The mentors you recruit will be directly responsible for the success or failure of the business incubator. Here are three absolute rules to follow when selecting your mentors.

- Mentors must actively be running a business or actively investing in businesses. Retired executives are not a good fit for this program.
- Professors make good mentors only if they have run successful businesses themselves. Their focus must be on business practice, not theory.
- You, the planner, are not a mentor. Unless you have run multiple successful companies, you are not a good fit.

Ideally, mentors will be mid- or late-career. Concentrate on finding people who run firms with 10 to 20 employees. These people will have more lessons to share with start-up companies than a CEO with a staff of 200 (unless that CEO grew the 200-person company from a start-up).

How do you find these people? If your area has venture capital firms or investment banks, ask people there. Members of these two groups might make good mentors, or they'll know other people who might be interested. Plus, these groups are inherently interested in new start-up opportunities in town. Other good sources of information are other business incubators, the chamber of commerce, business reporters, and university professors.

Business Incubators

Traditional Model Incubator

Focus: Subsidized Rent + Business Services

Cost to City: \$100,000–\$3 million

Typically Publicly Funded

Location Specific

Mentor-Model Incubator

Focus: Mentorship + Business Infrastructure

Cost to City: \$0

Typically Privately Funded

Physical Space not Required

Recruiting steps

To get started, commit to finding and meeting with one potential mentor a week either over coffee or during lunch.

At the meeting, explain the highlights of the mentor-model incubator: A group of successful business professionals will select, fund, and advise start-up companies. They will commit to at least two hours of mentorship a week for 10 weeks in exchange for a small ownership percentage.

Do a bit of homework on potential mentors. Then you can honestly tell them how you think their past success makes them a good fit for a mentor. Ask for their thoughts.

Be prepared for "I'm too busy," and follow up with "then that makes you the right person to teach young entrepreneurs how to manage their time." That said, graciously accept a "No." Your mentors must be committed and excited about the opportunity.

If you get "I'll think about it," give them some background information — a copy of this article or a printout of Paul Graham's thoughts about Y Combinator or the program description from the Capital Factory website. You'll have to take printouts, because busy people will forget to follow up when they get back to the office.

No matter what they say, ask them to recommend two other local business professionals that they admire.

As soon as the first mentor agrees to participate, ask that person to help you recruit other mentors from their network of contacts.

The number of mentors you'll need depends on the size of the business incubator, the number and types of businesses you want to help, and incubator goals. Some mentor-model incubators have four mentors; some have 20. Get more mentors than you think you will need, because inevitably one or two of them will drop out due to business emergencies.

Once you build your mentorship team, put all of your training as a planner and community organizer to work. Help the team set goals, create a plan, and determine a timeline. Identify potential problems: How will the team find companies, how long will the program be, how often will they meet with start-ups, and who will help the companies with the everyday challenges of running a small business (like when their Internet connection fails at 2 a.m.)?

Organizing business professionals will be somewhat like herding cats. Consider using surveys and conference calls to capture people's ideas. Give firm deadlines for responding and then move on if they don't meet a deadline. Also, consider asking the mentors to nominate one to three people as managing directors who will handle the logistics of the incubator program.

Here comes the hard part: Once your mentor team has a plan in place, gracefully bow out. But keep your eyes open as you are reading the morning paper or local blogs. Don't be surprised if you hear news that companies in the incubator program are hiring employees, launching new products, or going public. That's what happened after Paul Graham started Y Combinator, and it's what is happening today with PetsMD and Capital Factory. Over a few cups of coffee, you could help it happen in your city, too.

Kristen Carney is the cofounder of Cubit Planning, a start-up firm that was funded by a mentor-model incubator.

Resources

- Economic Development Administration: www.eda.gov
- United States Department of Agriculture; use the link for the Rural and Community Development Department: www.usda.gov
- National Business Incubator Association's Recession Resources: www.nbia.org/resource_library/recession_resources/funding.php
- See www.paulgraham.com for information about how to manage mentors.