

The Chinese University of Hong Kong



Entrepreneurship Ecosystem of Hong Kong

Interim Report

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INTRODUCTION

In worldwide rankings, Hong Kong has been listed in the top 10 innovation-driven and business-minded economies for many years. Its internationally competitive economy, solid information technology and communication policies, transparency and rule of law, coupled with the ease of doing business there, led us to believe support for local startups had gained momentum a long time ago.

In reality, the entrepreneurship support ecosystem of Hong Kong entered its growth stage only in 2009. Multiple institutions, incubators, co-working spaces, and other support organizations flourished after the worldwide financial crisis. According to our estimations, the number of local actors supporting entrepreneurs has at least tripled in the past 5 years. Have they begun to work together closely? Not yet.

This interim report draws a picture of the entrepreneurial ecosystem's growth and challenges. We explore the roles different actors play in the ecosystem and their contribution towards developing the local startup community. We investigate reasons why players in the ecosystem have not fully integrated with the other players in the community yet, and we lay down some implications for local entrepreneurship.

For the purpose of this report, we have identified 7 principal groups of actors. These are the entrepreneurial community itself, physical hubs, knowledge providers, government bodies, funding providers, public exposure enablers, and well-established industry members. While we discuss the first 5 groups in greater detail, the public exposure enablers, or media and startup contests and well-established industry members are only briefly mentioned in relationship to the other five.

We then complete the picture with a brief analysis of the state of entrepreneurial spirit in Hong Kong and demonstrate how innovative, high-intensity entrepreneurship programs, such as Empowering Young Entrepreneurs Program, fit into the landscape by enhancing the support ecosystem and by motivating entrepreneurs to act.

ENTREPRENEURIAL SPIRIT OF HONG KONG

There is little updated information available about overall entrepreneurship rates in Hong Kong. The last large-scale survey of the general population was conducted in 2009 within the Global Entrepreneurship Monitor study. In 2009, 3.6% of the adult population was involved in early-stage entrepreneurship, while 2.9% were entrepreneurs in established owner-managed companies, for an overall entrepreneurial activity totaling 6.53%. Compared to other countries, these entrepreneurship rates are considered to be low (though startup rate shouldn't be interpreted simply as a competitiveness ranking). For instance, in the same period, entrepreneurial activity in China was present in 35.66% of the adult population and in the US, in 13.68% of the same. More recent statistics from the 2011 Hong Kong Population Census provide some insight into overall entrepreneurial activity. In 2011, the percentage of working population (aged 15 and above) reporting their economic activity status as employers was 5.1%. Turning to youth entrepreneurship, a recent report from The Hong Kong Federation of Youth and Trade Development Council from 2014 revealed that the proportion of new entrepreneurs among young adults was 5%, up by 2 percentage points comparing to a similar survey from 2011. Considering the favorable environment for entrepreneurship praised in worldwide rankings, startup rates in Hong Kong are considered low. Even among university graduates, the level of self-employment in 2013 oscillated between 1.1% and 1.3% for undergraduates and taught postgraduates respectively.

Ironically, the entrepreneurial spirit of Hong Kong has remained dormant because of favorable economic conditions. While its hard-working society is open to novel situations, the memory of hardships experienced by previous generations combined with the availability of other, less-risky career opportunities have made Hongkongers approach entrepreneurship with reluctance. In the past, poor economic conditions made Hong Kong citizens rely on necessity-driven entrepreneurship. Older generations who survived difficult times want a different fate for their children and, in consequence, encourage them to enter less risky professional career paths. The abundance of non-entrepreneurial career opportunities acts in concert with the older generation's wishes and redirects Hong Kong's attention towards careers that do not involve starting new businesses. For the same reasons, it is difficult for local entrepreneurs to find a reliable and skilled workforce to support their endeavors and which would contribute to a spill-over effect where startup employees might turn to entrepreneurial careers themselves.

The cultural conditioning of potential local entrepreneurs becomes visible once they become more involved with the idea and join entrepreneurship programs. In fact, enrolling in entrepreneurship programs is a double-edged sword for people wishing to open their businesses. It helps to lay the groundwork for setting up the business, but it also tends to unleash more criticisms from family and friends. With increased pressure from loved ones, entrepreneurs become more sensitive to opinions from their closest peers. Through our survey we uncovered that those who decide to pursue entrepreneurial paths feel less pressured by negative opinions voiced by people important to them, which helps them to overrule these demotivating opinions.

ENTREPRENEURIAL COMMUNITY

These findings underscore the importance of support among fellow entrepreneurs and entrepreneurial networking groups, where new entrepreneurs can find the peer support they need to advance their businesses. Recent changes in Hong Kong's entrepreneurial ecosystem further strengthened the informal entrepreneurship networks of support, which, to some extent, provide a substitute for family and friend support in launching a business. Through interviews, we learned that in the most extreme cases, new entrepreneurs resort to changing their group of friends and replace past connections with fellow entrepreneurs. In their own words, their new goals and values are better understood and accepted by fellow entrepreneurs. The number of associations and groups related to entrepreneurial topics has tripled between 2008 and mid-2014. In addition to providing moral and advisory support to local entrepreneurs, these groups explore the multicultural aspect of the city and are getting better in promoting startup competitions and generating exposure for successful startup stories in the media.

PHYSICAL HUBS

The entrepreneurial community is particularly active in cooperating with physical hubs, where entrepreneurs can gather and share ideas. Physical hubs incorporate co-working spaces and government incubators. They create supportive environment to local startups and provide training, mentorship, networking, and financing opportunities. The first co-working spaces opened in Hong Kong in 2009, but the real boom took place in 2013, with 16 new spaces opening within the past 18 months. Although co-working spaces in Hong Kong have very well-established links to the startup support community and its associations, which ensure networking and learning opportunities for their members, their connections to potential investors and the media, which would increase local startups' public exposure and create funding opportunities, are rather scarce. The situation is quite different in government incubation programs. Cyberport and the Hong Kong Technology and Science Parks work closely with business angels and venture capitalists in providing investment to their incubatees. In 2013 alone, the cooperation between HKSTP and HKBAN brought a total of HK\$51.8 million to Science Park incubatees. 64% of interviewed experts consider government support programs such as science parks, incubation programs, and support agencies, as a strength of Hong Kong in promoting entrepreneurship. Our estimations suggest that in the years 2009-2012, 21% of new IT and telecommunications firms in Hong Kong were admitted to the government incubation programs. However, since the focus of incubation programs is mainly on the ITC sector, their capacity still falls short in having a significant impact on the startup population from other industries.

KNOWLEDGE PROVIDERS

Different types of physical hubs work with different knowledge providers. In terms of knowledge provision, universities are the most prominent source of learning opportunities for entrepreneurs. University-based entrepreneurship centers and programs, startup academies, and consulting and mentorship schemes account for 48.6% of all knowledge-related initiatives targeting entrepreneurs. A further 27% is covered by NGOs and government knowledge portals, support and mentorship programs, and startup academies, while 24.3% of knowledge-related initiatives are organized by private organizations, such as General Assembly or The Founder Institute. While co-working spaces are more connected to private knowledge providers, government incubators are mostly cooperating with local universities and NGOs.

According to our panel of experts, local universities have become better at fostering entrepreneurship in the past 5 years. Since 2010, universities have been particularly prolific in organizing entrepreneurship competitions, mentorship schemes, and incubation programs. Our experts also emphasized the introduction of common core studies, encompassing major interdisciplinary themes, as one of the elements with a potential to improve entrepreneurship in Hong Kong. For a long time,

Hong Kong's higher education has been criticized for being too focused on specific disciplines and discouraging cross-faculty cooperation.

As for industry spillover, the number of government-matched collaboration projects between the industry and universities has tripled since 2009 while direct funding from industry has grown by 34.6% in the same period. While local businesses support local universities by providing 11% of their research grants on average, US and Singapore businesses contribute only 5% of their universities' research grant money. However, the increased cooperation between universities and local businesses still needs to prove its impact on startup activity in Hong Kong.

GOVERNMENT BODIES

The involvement of government agencies in promoting entrepreneurship has both positive and negative aspects, according to our experts. On the positive side, they praise the simplicity of business registration rules, transparency of procedures, rule of law, prevalent learning attitude, community outreach, and the variety of support programs offered to entrepreneurs. On the negative side, "inadvertent" inefficiency, if not hurdles, of the government bureaucratic bodies in dealing with entrepreneurs were pointed out.

Setting up a business in Hong Kong is cheap, fast, and simple. According to World Bank's Doing Business Report, Hong Kong ranks as second economy in terms of the ease of doing business in 2014. It takes 2.5 days to start a business and there are 3 procedures involved in the registration process. In comparison to other countries, Hong Kong also has one of the most efficient and transparent economies in the world. For local entrepreneurs, this means that everyone is treated equally in dealing with government licensing, regulations, and procedures. Rules and procedures are straight-forward and clear and, in the case of novel situations, if well-justified with examples from other markets or other industries are presented (preferably from overseas), the government generally acts in favor of local entrepreneurs.

The "unwillingly inefficient bureaucracy" results from two principal dynamics. Firstly, policymakers are struggling to understand entrepreneurs' needs. For instance, the flexible exception regime in the copyright has not been introduced in Hong Kong although other countries' experiences have demonstrated its positive impact on the development of innovative internet services. Secondly, at the operational level, government officers have a limited understanding of strategic objectives for developing innovation in local industries, and sometimes create unnecessary obstacles to implementing new solutions in existing industries. The "not invented here" irony means that it is easier for local companies to get necessary licenses for out-of-the-box ideas adopted from other markets, than to get their own brand-new ideas approved. On one hand, the government is working hard to promote innovation and offers a wide range of funding opportunities to help local startups with patent applications, research and development funding, or consultancy. On the other hand, local bureaucracy sometimes inadvertently acts as an obstacle in commercializing and developing innovative business ideas.

FUNDING PROVIDERS

Accessibility to financial resources is still quite limited in Hong Kong considering we have one of the highest numbers of high net-worth individuals worldwide, and that we rank at 8th position in the 2013 Venture Capital and Private Equity Country Attractiveness Index. Our panel of experts pointed to the accessibility of financial resources as the most important weakness of Hong Kong's entrepreneurial ecosystem (64% of responses) and emphasized the contrast between their availability (abundant) and accessibility (very low).

In 2009-2013, Hong Kong has seen an outflow of startup investment, with HK\$ 10.5 billion being invested by local investors overseas and only HK\$ 3.7 billion being invested in local startups through seed, venture, and angel rounds, according to the CrunchBase database. Hong Kong-based investors mainly focused on investments in China, with 52.8% of funds invested over the past 5 years. Their investments in Hong Kong constituted 2.6% of all Hong Kong-originated early stage investments made in the years 2009-2013. Also, larger companies had a limited interest in investing in startups from their own industry, with only 3% of early stage investment deals coming from Hong Kong corporate investors. Access to financing options is limited mainly due to the size of local market, limited interest in cross-fertilization within local industries, reliance of personal referrals from business angels and family offices, and regulations on equity trade limiting crowd-funding operations.

In consequence, 60% of local startups launch their businesses with as little as HK\$100,000 of initial capital and mostly rely on self-funding. Capital-intensive Hong Kong startups with high growth potential are seeking funding from larger markets and are mostly funded with international capital, with the USA (44%) and China-based financiers (17%) as principal investors. Local early stage investors came in at 5th place, after France and Singapore, with funding available for only 6% local startups receiving high levels of capital. Loans from banks and government support were the least sought-after types of investments and the number of applications for government funds for entrepreneurs (SERAP) has declined since the inception of the fund in 2001.

Things are improving, however. The availability of financial resources has improved compared to 3-5 years ago, according to 44% of experts. The value and volume of early stage local investment has been rapidly increasing since 2011. Startup capital options in Hong Kong are expanding, with family offices becoming more interested in direct investment and crowd-funding platforms being developed locally, despite unfavorable regulations. There were 13 local crowd-funding platforms operating in Hong Kong in July 2014, 85% of them launched in the past 2 years. While government incubators have a long-standing history of cooperation with local investors, we also noticed several cooperation agreements that were recently established between co-working spaces and private investment groups.

REASONS BEHIND LIMITED COOPERATION

Why doesn't the ecosystem work together just yet? There are several reasons. Firstly, all of its elements are relatively new. Actors need to overcome the so-called "liability of newness" and they are still adjusting to the new environment and defining their roles. Secondly, they probably lack knowledge about the other elements of the ecosystem, and of their intrinsic value. Thirdly, they may simply not know how to communicate with each other and find synergies in their objectives. The above three factors cause the classic "coordination problem" when an economy or society seeks to move from an incumbent equilibrium to a better alternative. Lastly, given the low prospect of getting other necessary actors to make a move together, some of them may simply lack the motivation to create a better environment for local entrepreneurs. As individual actors cannot change the ecological system, smart actors in Hong Kong would not put in futile efforts. Thus, limited cooperation practices of the support environment, combined with cultural and social pressure to choose less risky careers, contribute to the lessening of the local entrepreneurial spirit. Conductors can weave musicians into an orchestra, and so can quartets who can self-coordinate, provided they can cooperate efficiently. Hong Kong needs both.

ENTREPRENEURS & STARTUPS OF HONG KONG

Considering the scarcity of data on entrepreneurs, we have developed profiles of the EYE Program applicants, who are new or potential future entrepreneurs. Consistent with findings from the 2009 GEM report, we focus on young entrepreneurs who constitute the majority of new entrepreneurs in Hong Kong. We admitted 902 new or potential entrepreneurs aged 35 or below to the EYE Program and collected data from 612 of them to describe in this report. Of these, 352 EYE Program participants decided to commit to launching a business and submitted a total of 148 business proposals that underwent a detailed analysis presented below.

Our typical entrepreneur is a Chinese male. He is between 21 to 25 years old and has already graduated from the university with a bachelor degree. He studied in Hong Kong and is quite versed in business. He feels strongly about his creative thinking and business management skills, but he wishes he knew more about fundraising. He briefly worked as an employee, but it wasn't for him and now he feels ready to start his own business. He already has an idea and a draft of his business plan, but has no experience in entrepreneurship and this is why he enrolled in the EYE Program. He is most probably looking for a teammate who can raise funds or is a programmer. A marketing person or user-experience designer would be a good addition to his team as well.

The typical EYE team is made of 2 to 4 persons (62.8% of all teams, including EYE and non-EYE members) with mainly male co-founders (62.2% are male-only teams), all being enrolled in the EYE Program (77.3% of teams with 2-4 members and 43.9% of total). Their expertise is mostly one-dimensional in business (31.8%) or combines business and technology (19.6%). They came up with the business idea during the program (87.2% projects are new) and it was a joint effort (83% not related to experience). Most of them had no external mentor or advisor to help them refine the business proposal (88.5%). They are looking for initial funding between HK\$ 100,000 and 500,000 (43%).

Their business idea is low-tech and rather mundane (69.6%), where they provide an online solution (84.3%) to an existing problem or industry. Examples include online trading platforms connecting more or less niche communities or businesses, traveling sites, networking apps, or location-based services. Most of them rely on B2B (32.6%), B2C (28.3%), or these two markets combined (34.1%) to increase their scope of activities and address the needs of global consumers (57%). The majority of businesses is planning to use a single revenue model (52.6%) and is focusing on advertising as the main source of income (55.6%). Subscription revenue models are the second most popular (36.8%) and are most commonly used in connection with advertising (9.8%).

AWAKENING THE ENTREPRENEURIAL SPIRIT

What makes young entrepreneurs take the leap and launch their businesses? Our study has shown that the way they perceive their environment and assess the startup ecosystem is essential to taking this first step. We asked 281 EYE Program participants about institutional factors that have positive or negative impact on their decision to become an entrepreneur, and we compared the responses of those who committed to entrepreneurial careers (198 persons) to those who decided to postpone it (83 persons).

Both groups were consistent in pointing out the top 3 factors influencing their initial decision to become entrepreneurs: availability of business opportunities and knowledge (73.5% of dropouts and 80.7% of committed), availability of funding sources for entrepreneurs (54.9% of dropouts and 66.5% of committed), and supply and use of technology and creative ideas (50% of dropouts and 62.7% of committed). However, people who committed to launching their businesses are more driven by support provided to their startups, while people who postponed their decision were more driven by their own preparedness and regulatory environment. A statistical analysis revealed that what also separates people who commit to launching a business from those who do not is their very different perception and influence of 3 factors, namely business incubation and mentorship, availability of funding for entrepreneurs, and ecology and environmental protection. Two competing stories emerged from the analysis, one about those who give up and the other one about those who launch their businesses.

Those who have given up would say "I wanted to launch a business and I had a great idea to commercialize (73% important; 80% positive). It was creative and technologically advanced (50% important; 94% positive). I am adequately educated to launch my business (41% important; 77% positive), but there were two major road blocks on my way. Firstly, there was not enough funding available for me to start up (59.4% important; 46% negative), and then the regulation and policies in Hong Kong are not favorable (45.1% important; 48% negative). Also, society is not very pro-entrepreneurship here (34% important; 37% negative) and the available business incubation and mentorship programs are still under development (32.4% important; 24% negative). It is even worse for those concerned with environmental protection and ecology – the business environment here is not favorable to them (24.5% important; 40% negative). Let me think again about launching my business and get some more education before I do it."

In contrast, those who committed to launch their businesses would say: "I want to launch a business and I have a great idea to commercialize (81% important; 89% positive). It is creative and technologically advanced (63% important; 92% positive). I took the decision to go for it because Hong Kong is such a positive environment for setting up a business. It has a good choice of business incubators and mentorship programs (56.7% important; 91% positive), viable financing options (66.5% important; 77% positive), and a society that is rather supportive of entrepreneurship (47.6% important; 70% positive). Also, for those interested in the ecology and environmental protection, it is full of opportunities (27% important; 81% positive). I am a little bit worried about whether I will get as much funding as I need (23% negative) and about all the regulatory issues (46.4% important; 36% negative), but I am confident my education is good enough for me to deal with these issues (42% important; 88% positive). Let's do it!"

ROLE OF EYE PROGRAM

Entrepreneurship programs, such as EYE Program, are specifically designed to help to address specific challenges resulting from the ecosystem development stage, not-so-favorable social norms, and entrepreneurs' needs. We see our role as a *provider of diverse new entrants to the ecology and an ecosystem broker promoting interdisciplinary cooperation, helping to connect, and enhancing existing connections in the entrepreneurship support network.*

At the ecosystem level, the EYE Program was conceived to help build connections between the investors, well-established industry members, the media, and physical hubs. A university-based program became a platform where these players come together to help a large number of local startups and guide them through the gestation activities. We brought investors and industry players to startups, startups to co-working spaces, and media attention to everyone with the intention of promoting local creativity and innovation, inspiring intra-industry interaction and cross-fertilization, and increasing industry and public exposure of local startups. The EYE Program, as a credible voice, rallies and empowers all actors in the ecology to charge ahead, in Cantonese “吹雞” — meaning let’s gather to accomplish. As a matter of interest, “吹雞” is also used as a name by one of the EYE startup teams.

In terms of alleviating pressures resulting from social norms, our program provides support to individual entrepreneurs in enabling their interactions with mentors and creating a community within the program that rides on the wave of self- and inter-peer motivation. We have connected many “wannabe” entrepreneurs and helped them to overcome mental and social barriers to entrepreneurship by helping them to embark on the entrepreneurial journey. Through the EYE Program, they are getting to know their own strengths better, meeting others with a similar drive, connecting and forming teams, and coming up with almost 150 ideas for new businesses. Business ideas aside, these few hundreds of youngsters shall continue to be active in entrepreneurship in the years to come.

Finally, in addressing the needs of new entrepreneurs, we provide them with mentorship support, so sought-after by those who decide to launch their businesses. We also encourage them to form interdisciplinary teams, because we understand how important it is to any startup to draw on multiple domains of knowledge and industries in creating sustainable businesses.

So far, the EYE Program has been successful in achieving its entrepreneurial learning objectives, even with the expectations bar set very high from the beginning. Overall, participants confirmed the program improved their intention to implement the business idea (76.5% agree about the outcome, with a slight increase between expectations and outcomes of 1.1 percentage points among those who disagree) and increased their understanding of the attitudes, values, and motivation of entrepreneurs (77.9% agree about the outcome with 2.9 percentage points increase between expectations and outcomes among those who disagree). Participants are the least satisfied with the enhancement of their practical management skills in order to start a business (7.5% disagreed about the outcomes with a 7.1 percentage point increase between expectations and outcomes in those who disagree). A further breakdown by the commitment levels to the program reveals that people who are more committed and submitted their business proposals to further participate in the EYE Program had higher levels of objectives’ fulfilment than those who dropped out.



If we were to describe Hong Kong’s entrepreneurial ecosystem with the use of startup theory, it has just performed a mostly successful commercialization and is now in its growth stage. Hong Kong is waking up, as one of our experts said, and it is doing it with its well-known dynamism and drive. What’s the next step? The synergy in the startup support ecosystem needs to catch up in order to optimally energize the dormant entrepreneurial spirit.