Influence of Government Intervention on Strength of Entrepreneurial Ecosystems

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Abstract

Using case studies from developed economies like the United States, the paper evaluates how direct and indirect government intervention can impact the entrepreneurial ecosystem. Quantitatively, data from OECD and the World Bank will be used to explore correlations between government intervention and indicators of ecosystem vitality. This will be measured through startup density, venture capital activity, and startup survival rates. Sustainable entrepreneurship will also be examined, particularly the government's position in leading the green movement.

The paper aims to model the optimal environment for startups and SMEs, investigating government interventions ranging from direct venture management to regulatory frameworks. By comparing the two types of interventions, the paper argues that the government's most effective role in the entrepreneurial sphere is increasing institutional quality rather than managing venture capital funds.

Introduction

The government plays a decisive role in shaping the entrepreneurial environment through interventions that influence innovation and the conditions for firm growth. This paper will divide the types of interventions into two main categories: direct venture management and regulatory frameworks. Direct venture management refers to the government managing venture capital funds and increasing capital supply to businesses in order to strengthen the entrepreneurial atmosphere and encourage innovation ("What is"). Regulatory frameworks, on the other hand, consist of the government improving institutional quality through policies such as lowered taxation and subsidies as incentives for startups to keep producing and thus maintain the entrepreneurial ecosystem (David et al.).

However, neither type of government intervention comes at a low cost; both require the government to contribute large amounts of money. This gives rise to the research question, "To what extent does government intervention influence the strength of entrepreneurial ecosystems in developed economies?" to explore whether the high costs are worth it and which types of intervention should investment be prioritised due to cost-benefit ratio.

1. Hypothesis

My hypothesis is that government intervention influences the entrepreneurial ecosystem to a large extent, with regulatory frameworks wielding a larger positive impact compared to direct venture management. This is because regulatory frameworks can set a more sustainable entrepreneurial environment in the long run, while direct venture management can be beneficial in the short-term as a boost for startups (Sharma and Subba).

2. Background

The entrepreneurial ecosystem describes an interdependent network of actors and factors in the economy that collectively support startups to launch and scale. Such ecosystems operate bottom-up, driven by entrepreneurs to innovate and sustain creative ventures (Stam and van de Ven).

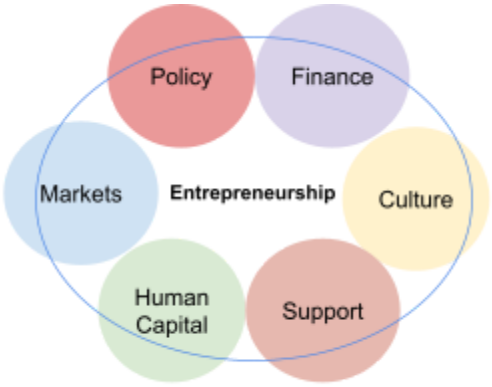

Figure 1. Isenberg's six domains of an entrepreneurship ecosystem (Fuerlinger et al.)

Economist Daniel Isenberg researched the entrepreneurial ecosystem, and identified 6 key domains that make up its success: finance, policy, culture, support, human capital, and markets. This paper focuses on the policy domains, which support the ecosystem through two main angles: covering the gaps in specific actors and improving framework conditions. Each ecosystem is unique and requires tailored interventions from the government.

Recent research shows that venture management and regulatory frameworks from the government are key elements that act as the backbone for the "policy" domain in the entrepreneurship ecosystem. Strong interventions and efficient public administration reduce uncertainty, lower transaction costs and crowd in private investment. On the other hand, poorly designed frameworks introduce distortions and lower startup vitality rates, which refers to the general survival rate of new enterprises in a country.

3. Methodology

To measure the success of each type of government intervention, this paper will explore both quantitative and qualitative data on regulatory frameworks and venture management. A general picture using the top 10 global entrepreneurial ecosystems will be created, which will be used to analyse patterns. Qualitatively, this paper will use secondary sources to analyse key features of each type of intervention through interviews.

The **independent variable** will be the regulatory frameworks or venture management being implemented. Regulatory quality will be measured using the regulatory quality index (1 means highest quality and 0 means lowest quality) (Globalen LLC). Venture management will be measured by the venture capital investments index ("VC investors, deal count/bn").

The **dependent variable** will be the strength of the entrepreneurial ecosystem as measured by new business density rate and ecosystem vitality rate ("World Bank Open Data").

4. Quantitative Data

To better understand the difference in impact of regulatory frameworks and venture management as government interventions, I will compare the two variables for the top 10 entrepreneurial ecosystems in the world, ranked based on market performance and reach, funding, and AI-native transition: United States (Silicon Valley), United Kingdom (London), Israel (Tel Aviv), China (Beijing), Korea (Seoul), Singapore, Japan (Tokyo), France (Paris), India (Bengaluru-Karnataka), and Canada (Toronto) (The Global Startup Ecosystem Report 2025). Using the data captured in Appendix A, the following graph was

formulated. The entrepreneurial ecosystems are graphed in order of their strengths, with Canada being the lowest of the list, and the US being the highest. The blue datapoints represent regulatory quality, the red datapoints represent new business density, and the yellow datapoints represent venture capital investments.

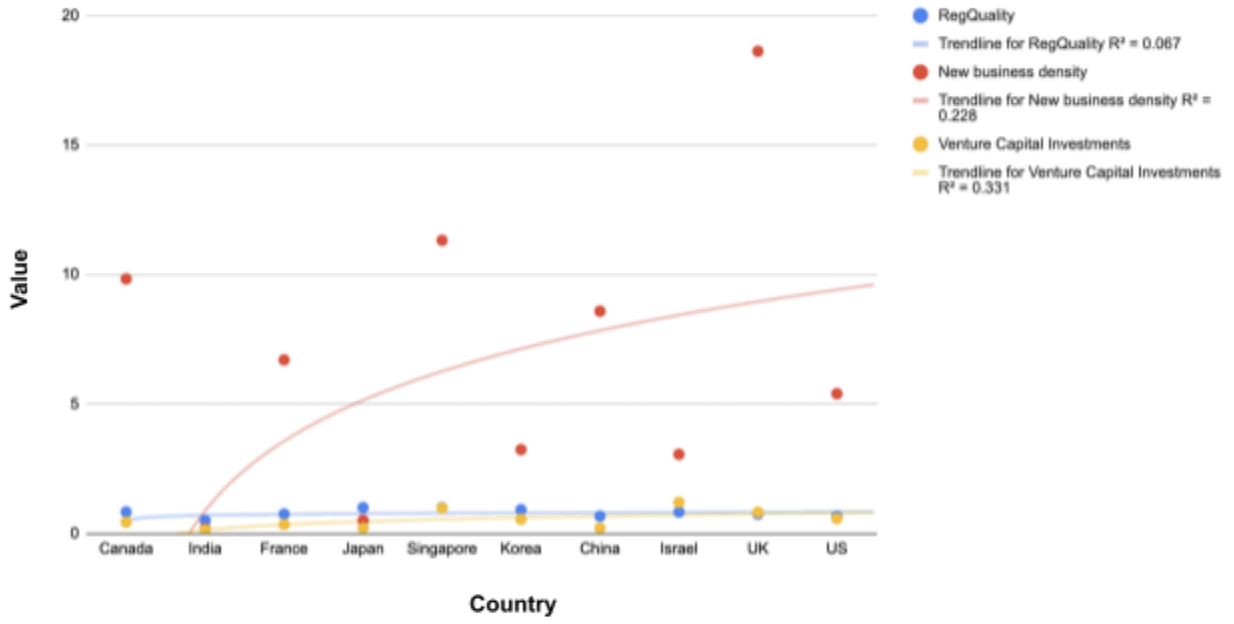

Figure 2. Top 10 global entrepreneurial ecosystems' regulatory quality and venture capital investments against new business density

By observing Figure 2, it is hard to indicate which variable specifically influenced the entrepreneurial sphere more, since both venture management and regulatory frameworks were implemented in the same time period, so no independent variable was established, meaning no correlation can be identified. In fact, venture management and regulatory quality showed a consistent rate in all countries, being similar among all countries. However, venture capital investments showed a positive trend, increasing as the strength of the entrepreneurial ecosystem increased, meaning those economies invested more in venture capital. Similarly, the new business density increased with the strength of the entrepreneurial ecosystem as well. However, it is worth noting that the R^2 value was only 0.228, meaning only approximately 23% of data matched the trendline. This means that there is little to no correlation between the variables, and the data does not fit the trendline in a meaningful sense.

However, Figure 2 provides certain indicators to draw conclusions. The graph demonstrates certain patterns where countries with high regulatory quality but only moderate levels of venture capital still have solid new-business density, such as the UK, France, and Canada. Moreover, countries such as China and India have high venture capital but poorer regulatory quality, yet do not have proportionally higher new-business density. This highlights that good institutions can compensate for less public capital, whereas capital alone does not guarantee the entry of a lot of new firms.

Regulatory reform

To analyse the effects of regulatory frameworks more closely, the auto-entrepreneur regime in France is examined. In 2009, the French government streamlined the process of running small businesses and revolutionized self-employment. To do so, they allowed enterprises to pay social charges and taxes based on a fixed percentage of actual turnover (0% if no income), with simplified registration and no initial VAT registration. These features lowered the entry barrier for new enterprises, acting as an incentive for this business regime to boom ("The Auto-entrepreneur").

Following the regulation, between 270,000 and 360,000 auto-enterprises were created annually, accounting for more than half of the business start-ups in France. This sharp surge in new firm registrations following the reform suggests that lowering administrative and fiscal barriers can have an immediate and effective influence on business creation, emphasising that regulatory frameworks are a powerful catalyst for strengthening entrepreneurial ecosystems in developed economies.

Venture capital management

On the other hand, government-managed venture capital (GVC) typically demonstrates less of an effect, especially when compared against independent venture capital (IVC). Specifically, researchers Grilli and Murtinu utilised a longitudinal dataset of high-tech firms across multiple EU countries and found that GVC had no significant positive effect on employment growth and firm sales; whereas IVC, which isn't managed by the government, demonstrated a robust positive impact on sales growth (2014). This trend is also present in other studies, where researchers have described a lesser impact of GVC on entrepreneurship when its influences are compared to IVC.

This implies that, even in periods when the government substantially expands their GVC, it only has an incremental effect on firm-level performance, which is negligible compared to that of market-driven angel investors. Since GVC costs a significant sum of money, concerns can arise regarding whether the funds can go elsewhere and create an even larger impact, such as by reinforcing regulations.

5. Qualitative Data

In a study by Owen and Vedanthachari, 51 interviews were conducted to study UK government support for university-based cleantech finance (2023). Entrepreneurs who participated in this research expressed that the government budget is most useful in strengthening the entrepreneurial sphere when it funds infrastructure, grants, and regulations, while leaving investment decisions to private seed funds and IVC. This is because long-horizon and integrated policies are more valuable than the government trying to pick individual winners.

Other than regulations, the government interference that establishes infrastructure and opportunities for innovations were also seen as beneficial. Bramwell, Hepburn, and Wolfe worked on a case study on the Ontario Network of Entrepreneurs that ran for 20 years, highlighting that the regional innovation centers built by the Canadian government were effective in connecting firms, universities and investors (Bramwell et al., 2019). By developing intermediaries for firms, the entrepreneurial ecosystem was further strengthened as there were increased pathways for opportunities, investments, and collaboration.

Using such secondary sources and methods like interviews and case studies, the appeal for regulatory frameworks become increasingly larger, stressing the positive influence it can have on the entrepreneurial sphere.

6. Discussions

Based on the qualitative data, it is apparent that government interventions influence the strength of entrepreneurial ecosystems in a significant manner. Specifically, regulatory frameworks implemented by governments appear to wield a stronger effect on entrepreneurship compared to direct venture management. A potential explanation could be that regulatory frameworks shape the baseline incentives and constraints that entrepreneurs operate under, whereas venture capital only reaches a small set of firms at the growth frontier since the government chooses firms to invest in. Strong regulations also target various areas that provide security for startups, such as implementing rules around contract enforcement, taxation, or product standards, reducing uncertainty and transaction costs for every new firm, thus making entry less risky. In contrast, increases in available venture capital only affect firms that are already investment-ready. Without stable regulation, venture capital cannot wield enough impact since investors may either demand higher returns, concentrate in safer sectors, or just opt out of investing. This leads to capital being unable to translate to business creation, defeating the purpose of such interventions. Thus, regulatory frameworks act as a foundation that allow capital to be deployed efficiently, which is why ecosystems with strong institutions but only moderate venture funding, like the UK, can sustain new-business formation.

However, the same correlation is difficult to identify from the quantitative data, with the trendline and its R^2 value demonstrating an extremely weak correlation.

Despite this, Figure 2 can still act as an indicator of a correlation, where countries with high regulatory quality and only moderate venture capital continue to have steady new business density, while countries with high venture capital and low regulatory quality do not necessarily have proportionally higher new business density. This suggests that while both are essential in maintaining a healthy entrepreneurial ecosystem, regulatory frameworks create a larger positive impact. However, the quantitative data is suggestive, but not robust, so no real correlation can be drawn.

Ideal entrepreneurial ecosystem

According to the research, this paper argues that the optimal startup environment would be one where the government distributes more resources into regulatory frameworks than venture capital management, yet still devotes efforts into both. An ideal environment would consist of simple administrative processes to lower the entry barrier, encouraging new businesses to enter the industry. Taxation would also be low for firms, acting as a financial incentive and allowing firms to have more capital to work with since they can spend less on tax. The government can also implement schemes and grants to encourage high-performers of the industry, allowing for additional investments in research, skills, and infrastructure, instead of large GVCs. Intermediaries that connect firms to universities, corporates, and investors can also be established to provide an additional channel for firms to seek opportunities. Meanwhile, the government can still manage capital by shifting from picking specific firms to invest capital in, to partnering with private investors, rather than running GVCs. Governments can run co-investment schemes where public money automatically follows deals led by independent venture capital firms or angel investors. They can also provide early seed grants to firms through competitive selection processes to encourage innovation. In doing so, a stable and adaptive environment where private entrepreneurs and investors can coordinate efficiently can be established, effectively strengthening the entrepreneurial ecosystem of an economy.

Furthermore, sustainability has become increasingly important, particularly in entrepreneurship. The government can also take note of this and incorporate more regulations regarding green startups. For

example, Carbon Contracts for Difference (CCfDs) is an intervention that invests in low-carbon technology, encouraging firms to switch to it from unrenewable resources (Canestrini, 2025). Germany has been a pioneer in this movement, having invested €5 billion into their 15-year CCfDs program for industrial decarbonization (European Commission, 2025). Moving forward, such interventions that advocate for sustainability can be increased, creating a green movement and ensuring future generations have the same resources.

7. Reflections

While regulatory frameworks are more effective than venture capital management on their own, they still contain the limitation of being structural but indirect levers that cannot guarantee how stakeholders respond. Well-designed interventions can lower barriers and uncertainty, yet they do not ensure a sufficient supply of strong networks, early-stage risk capital and entrepreneurial skills. These regulations also take time to implement and adjust to political cycles, so they may generate unintended consequences if poorly coordinated.

Venture capital management is helpful in lowering entry barriers, yet contains the limitation of being costly to implement, and also the government "picks winners", which provides firms an unfair advantage or disadvantage. Firms chosen for support may grow and succeed more due to political priorities than their actual innovation potential, in contrast to more capable firms not selected which may struggle to find funding, leading to a misallocation in resources and potentially weaken overall market performance.

Research

My quantitative data used the top 10 entrepreneurial ecosystems in the world, which is not globally representative; it can be considered an overgeneralization. Also, since the dataset was small, the data showed little to no correlation, with one of my R^2 values being 0.067, which is very low and indicates a majority of the data does not fit the trend. With only 10 datapoints, I would need an exceptionally high R^2 value and very low p-values, both of which this paper lacks. Therefore, the sample size and correlation acts as a central constraint to this research, and no meaningful conclusion can be drawn from this data collection.

My qualitative data was collected through secondary sources, gathered using interviews and case studies, both of which leave room for error. The validity and reliability of interviews can be hard to determine since interviewees may be biased and influence test results. The sample was moderately-sized, with 51 interviewees, sufficient though a larger dataset would be better to draw conclusions from and minimise data uncertainty.

8. Conclusions

Given the drawbacks from the research method, where a correlation is difficult to establish given the limited sample size and low R^2 value, this paper acts in support of other literature that argues government interventions influence the strength of entrepreneurial ecosystems to a large extent, yet cannot confidently conclude this given the weaknesses in quantitative evidence gathered. Despite this, qualitative evidence suggests regulatory frameworks are more effective than venture capital management.

Appendix A. Global Regulatory Quality and Venture Capital Investment against New Business Density

	Regulatory Quality (Globalen LLC)	Venture Capital Investments ("VC investors, deal count/bn")	New business density (World Bank Open Data)
Canada	0.83	0.44	9.8
India	0.5	0.14	0.2
France	0.75	0.35	6.7
Japan	1	0.21	0.5
Singapore	1	0.98	11.3
Korea	0.92	0.55	3.2
China	0.67	0.21	8.6
Israel	0.83	1.2	3.1
UK	0.75	0.82	18.6
US	0.67	0.58	5.4

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