

Effects of Institutions and Policies on Entrepreneurship

Examples of macro and micro policies, their intended objectives, and unintended consequences.

Policy	Description/examples	Objectives	Unintended consequences
Macro policies	Institutional environment—rules of the game	Create environment in which entrepreneurship and innovation can flourish	Helps large as well as small ventures Does not target key industries or technologies Often slow and difficult to change
Property rights protection	Low risk of nationalization/appropriation Low rate of property crime Intellectual property protection	Encourage investment and new venture formation Encourage discovery and creation of new products and services	Strong IPR can encourage overinvestment in legal protection, excess litigation costs
Well-functioning legal system	Contracts enforced Legal disputes resolved smoothly	Facilitate economic exchange Enhance societal trust	
Free and open markets	Minimal interferences with market prices Minimal state-granted monopoly, entry barriers Minimal licensing restrictions Antitrust legislation	Encourage entry of new firms Curtail incumbents’ ability to hamper competition	May fail to address negative spillovers related to specific industries (e.g. tobacco, alcohol, medicine)
Regulations	Processes for licensing and certification of new products, services, and technologies Mechanisms to establish standards and adjudicate issues	Promote consumer and environmental safety while (1) easing pathways to receive approvals (2) removing or reducing barriers to compliance	Allow new and unintended applications of the technology Favors well-funded and connected firms Certification signals not completely accurate about underlying quality
Tax code	Predictable and transparent taxation Entrepreneurial risk not overly taxed Investments in startups not overly taxed Startup-friendly stock option legislation	Encourage startups at larger minimal efficient scale Encourage working for startups Encourage investments in startups	May encourage opportunistic tax planning
Labor legislation	Prohibit non-compete covenants Make retirement and health care costs independent from employer Easy-to-hire, easy-to-fire legislation	Lower ‘switching costs’ from employment to entrepreneurship Facilitate staffing in startups	May jeopardize workers’ rights
Stable monetary system	Low inflation Predictable central-bank behavior	Encourage domestic and foreign investment Reward long-term orientation Facilitate economic calculation	Limited discretionary monetary policy to deal with crises
Efficient bankruptcy code	Exemption rights (limited personal liability for business debt) Reconstruction process of failed enterprises	Allows resources to be allocated from lower- to higher-valued uses	Costly to workers and other stakeholders of bankrupt ventures
Low business registration costs	Few required permits to launch venture Fast processing of new business registrations	Encourages new venture formation	May encourage risky or low-quality ventures
Micro policies	Intended to boost new forms of innovative entrepreneurship and support recipients who are unable to access resources through conventional markets	Allow targeting of key firms, technologies, and industries	Inefficient at picking winners Can encourage rent seeking / crony capitalism Difficult to evaluate / scale
Financial incentives	Cash subsidies Tax incentives	Enable entrepreneurship and innovation that otherwise would not have occurred or been as innovative	May select or certify entrepreneurs who would have been successful anyway
	Government-administrated risk capital (e.g., Government Venture Capital) Competitive grants Loan schemes		May distort competition by sponsoring low-productive firms
Indirect subsidies	Incubator and accelerator sponsorship Science parks	Facilitate venture innovation and growth Facilitates clustering of complementary ventures	May select entrepreneurs who would have been successful anyway May distort competition by sponsoring low-productive firms
Training programs	Entrepreneurship mentoring Entrepreneurship education and training Advising and networking	Enhances human capital	Costly at large scale May encourage low-quality ventures
Contingencies and complementarities among conditions	What micro policies work better under specific institutional conditions? How do micro policies affect institutions? How do policies interact within levels?	Make policies more effective by leveraging interactions	Costly to design and evaluate specific policies for every context

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