JOURNAL OF RESEARCH PERSPECTIVES IN MULTIDISCIPLINARY SCIENCE, EDUCATION AND TECHNOLOGY (RPSET)
VOL: 1, ISSUE 4, OCTOBER – DECEMBER 2026
RCHUB PUBLISHER
ISSN: 3139-3934
DOI: https://doi.org/10.65725/RPSET/1/4/004

THE INFLUENCE OF ENTREPRENEURIAL ECOSYSTEMS ON THE GROWTH AND SUSTAINABILITY OF STARTUPS AND SMEs

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ABSTRACT

In the highly dynamic and competitive business landscape today, the entrepreneurial ecosystem has emerged as a crucial factor in the success of new ventures and small-to-medium enterprises (SMEs). This study looks at the complex interdependence between the different components of the ecosystem and the growth of these enterprises. We have engaged in different empirical studies in several countries to identify how access to capital, mentorship, networking opportunities, government policies and other cultural factors interact and influence the performance and survival of start-ups over time. We found that the entrepreneurial ecosystem is a network of resources, people and institutions that work together, either supporting or inhibiting, entrepreneurship activity within an ecosystem.

Specifically, our results show that the availability of capital and quality mentorship is strongly correlated with the growth rate of a new business, and that the synergy of the three support groups (the university, the customer and the supplier) amplifies the potential of value creation of SMEs. Moreover, the presence of government support programs such as incubators and entrepreneurial certification institutions gives investors a sense of the future of new businesses. Nevertheless, new ecosystems also encounter difficulties such as fragmented policies, a dearth of initial funding for their first phase, and being clustered in a small area. This study reveals the need for collaboration among all stakeholders to provide the necessary skills necessary to create an ecosystem conducive to sustainable growth, by contributing financial, human and institutional capacity and a welcoming regulatory environment. Policy and institutional measures will be critical at both these levels to take strategic steps to make the ecosystem more effective overall, and thus more inclusive for entrepreneurial opportunities.

Key words - Entrepreneurial Ecosystem, Small and Medium Enterprises (SMEs), Access to Capital, Mentorship and Networking, Government Support Programs.

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1. Introduction

Entrepreneurship is recognized as one of the great drivers of economic growth, job creation and innovation in both developed and developing countries. However, a founder's efforts to build a new business and small-to-medium enterprise (SME) are not the only factors that will determine whether the new venture or SME lives or dies. In the last fifteen years or so, the importance of the "entrepreneurial ecosystem" to the understanding of why entrepreneurship is higher in certain regions of the world, but not others, has grown in prominence (Isenberg, 2010; Stam, 2015). An entrepreneurial ecosystem can be understood as a set of interdependent actors and factors - entrepreneurs, investors, mentors, universities, government agencies, customers, and suppliers that are coordinated in a manner that enables productive entrepreneurship within a given territory (Stam, 2015; Acs, Stam, Audretsch, & O'Connor, 2017).

This paper looks at the interaction of the different ecosystem elements in relation to each other and how they influence the start-up and SME growth path and sustainability. Instead of looking at the elements of access to capital, mentorship, networking and government policy, and culture as independent variables, we see them as inseparable components of one system whose configuration enables or impedes entrepreneurship development in a specific community. It reviews the wide range of empirical and conceptual research in various national contexts, collates the evidence on functioning of the ecosystem, pinpoints the specific mechanisms by which the elements of the ecosystem contribute to the outcomes of the firm and points to the structural limitations to ecosystem effectiveness that remain. The paper is organised as follows. In section 2, the theoretical background of the concept of entrepreneurial ecosystem and its components are reviewed. The methodological approach is outlined in Section 3. Section 4 reports the results and reflects on the impact of capital, mentorship, institutional support and government policy on the effectiveness of start-ups and SMEs, as well as the ongoing problems that ecosystems encounter. Section 5 suggests a co-operative approach to sustainable ecosystem growth, Section 6 looks at policy issues and Section 7 concludes.

2. Literature Review and Theoretical Framework

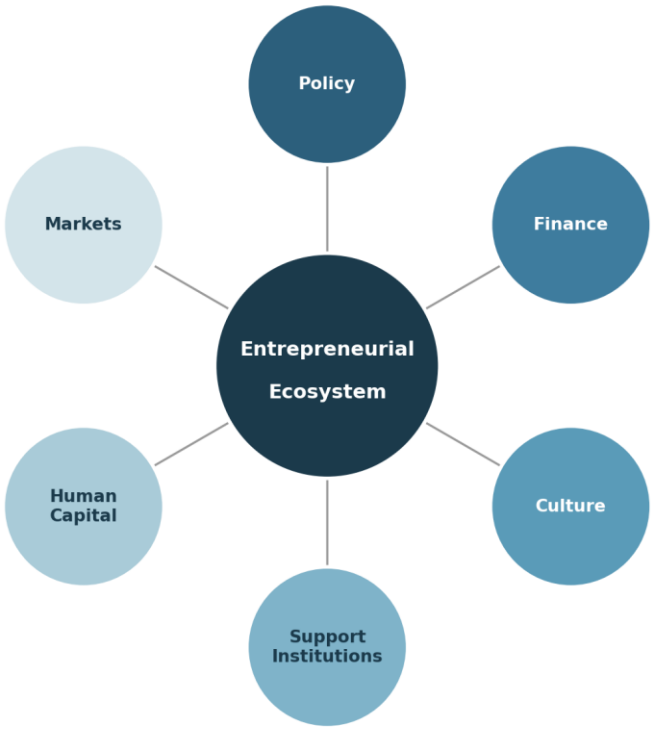
2.1 Conceptualizing the Entrepreneurial Ecosystem

The entrepreneurial ecosystem metaphor originated from a previous series of research and publications on regional innovation systems and industrial clusters, but was popularized by Isenberg's

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(2010) Harvard Business Review article, 'How to Start an Entrepreneurial Revolution' among researchers, practitioners and policy makers. To encourage entrepreneurship, Isenberg (2010, 2011) suggested that governments should not try to copy Silicon Valley as it exists in its entirety, but rather build an entrepreneurial ecosystem specific to their local circumstances, with six components – policy, finance, culture, support institutions, human capital and markets. Based on this, Stam (2015) made a more elaborate synthesis, highlighting the two levels of the entrepreneurial ecosystem: the systemic conditions (networks, leadership, finance, talent, knowledge, and support services) and the framework conditions (formal institutions, culture, physical infrastructure, and demand) that underlie it.

Figure 1. Isenberg's Six Domains of the Entrepreneurial Ecosystem



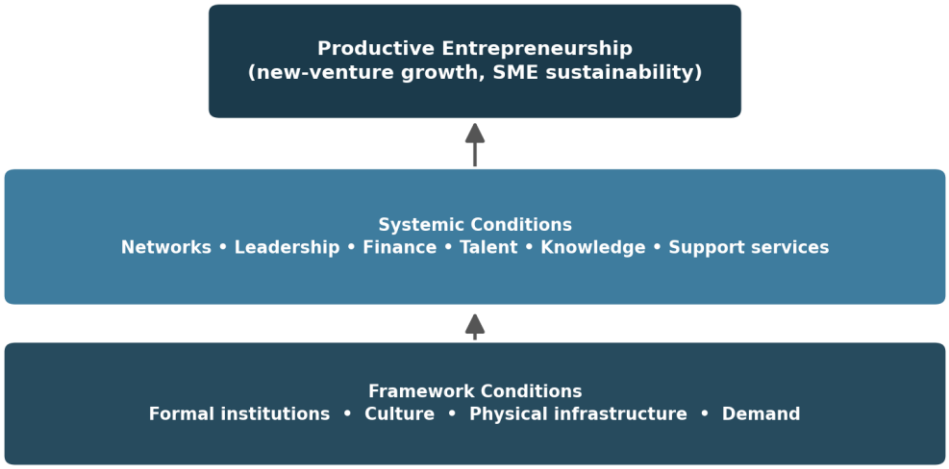
Source: adapted from Isenberg (2010, 2011).

Follow-up studies have focused on the relational nature of ecosystems as it defines value creation as a result of the quality of relationships between actors (Spigel, 2017; Acs et al., 2017). Importantly, as Spigel (2017) demonstrates, entrepreneurial ecosystems are a set of cultural, social and material characteristics that are mutually reinforcing; a strong mentorship culture, for example, is likely to enhance the efficiency with which capital and market access is translated into venture growth. Following this line of thought, Malecki (2018) also conceives of entrepreneurship as a local, place-based practice, while also recognising that it relies on resources and networks outside of the local

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community. While, at the same time, Brown and Mason (2017) warn that the concept of an entrepreneurial ecosystem has sometimes been used too broadly, stating that research should be more careful to differentiate between the underlying conditions of the ecosystem and the products it is said to be capable of producing, to ensure that the concept remains explanatory in nature rather than being stretched to cover any supportive business environment.

Figure 2. Stam's (2015) Framework and Systemic Conditions of the Entrepreneurial Ecosystem



Source: adapted from Stam (2015).

2.2 Core Components of Entrepreneurial Ecosystems

Although the terminology used is somewhat different from study to study, the literature comes together and suggests a fairly consistent set of components of an ecosystem. Mason and Brown (2014) cite finance, a group of experienced entrepreneurs ready to invest their time and money ("entrepreneurial recycling"), and an environment rich in information as other key attributes of ecosystems that generate high-growth firms. Acs, Autio, and Szerb (2014) formalize these in a "national system of entrepreneurship", positing that it is the efficiency of this interaction that constitutes the most important factor, along with resource allocation, in the institutionalization of the individual-level attitudes, abilities, and aspirations. Autio et al. (2014) build upon the framework by highlighting how the extent to which entrepreneurial innovation is realised in commercial outcomes is influenced by ecosystem context, the extent to which institutional voids are filled, and the maturity of intermediary organisations, as well as local demand. Audretsch and Belitski (2017) extend these

concepts to the city level, and find that culture, formal institutions, infrastructure, digital connectivity, workforce diversity (the "melting pot" effect) and local demand all converge to account for differences in entrepreneurial activity across a sample of European cities. Lastly, Cohen (2006) broadens the scope of the ecosystem concept to sustainability, suggesting that formal and informal networks, physical infrastructure and culture can be intentionally structured to foster sustainable VCs over time, which is the focus of the present study.

3. Methodology

The overall approach of this study is a qualitative and synthesis-based approach, based on an integrative empirical and conceptual analysis of the literature on entrepreneurial ecosystems, start-up growth and SME sustainability. The paper aggregates the results of empirical studies carried out in a range of national and regional settings, using a variety of methods, such as the use of large sample analyses at the regional level, city-level structural equation modelling and case studies of individual ecosystems, to uncover commonalities in the relationships between the various components of the ecosystem and the outcomes of the process. Sources were chosen because they made a contribution to the theoretical development of the entrepreneurial ecosystem construct (e.g., Isenberg, 2010; Stam, 2015; Spigel, 2017) or their empirical treatment of specific components of the ecosystem, including finance, mentorship, university linkages, and government policy (e.g., Mason & Brown, 2014; Audretsch & Belitski, 2017; Acs et al., 2014). Results were then grouped thematically, under the following five ecosystem dimensions which were found consistently across the literature: Financial capital, Human capital and mentorship, Institutional and market support, Government policy and Ecosystem level constraints. The integrative approach makes it possible that the study captures regularities in the functioning of ecosystems across the country while keeping an eye on the contextual variation typical to entrepreneurship research.

4. Findings and Discussion

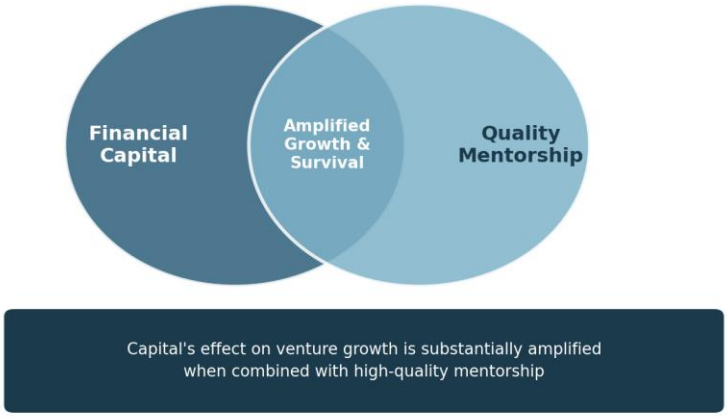
4.1 Capital and Mentorship as Growth Drivers

In all of the studies that have been reviewed, financial capital availability is generally among the strongest factors shown to correlate with growth of new ventures. But the evidence is also clear that it isn't just about capital – it's also about quality mentorship, which clearly enhances the

ISSN: 3139-3934
DOI: https://doi.org/10.65725/RPSET/1/4/004

impact of capital on growth. Mason and Brown (2014) explain that mature ecosystems can be enhanced through "entrepreneurial recycling", which can involve capital, tacit knowledge, networks and mentorship being passed from exited entrepreneurs to the next generation of founders.

Figure 5. Capital and Mentorship as Complementary Growth Drivers



Source: developed from Mason & Brown (2014) and Spigel (2017).

This financial and human capital transfer is a possible reason for start-up survival and scaling to be so different in regions with similar venture funding levels. This is also confirmed by Spigel's (2017) relational approach; where he found that mentorship and informal exchange of knowledge can be a different form of resource and, in some instances, a more powerful asset than direct financial capital, as it can help entrepreneurs to better understand market signals, fine-tune their business models, and improve their chances of avoiding common execution pitfalls in the early years that directly impact the success of a business venture.

4.2 University, Customer, and Supplier Support and Value Creation

The second consistent result relates to the contribution of non-financial institutional actors' universities, customers, and suppliers to increasing the value-creation potential of SMEs. Universities bring talent and catalyse applied research whilst customers and suppliers offer market feedback, early revenue and operational capacity that pure financial investors can only rarely replace; in many ecosystems, universities also supply formal technology transfer and incubation structures.

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Audretsch and Belitski (2017) tested the ecosystem view by analysing how well European cities did in fostering entrepreneurial activity and found that the coordination of actors is more important than the formal institutions or the demand environment alone, as both were equally good at predicting the level of entrepreneurial activity. SMEs seem to be more successful in turning innovative ideas into commercial products and services when universities, customers and suppliers are part of a coordinated support network instead of disenfranchised stakeholders.

4.3 Government Programmes, Incubation and Signalling Effects

Besides the direct contribution of these support programmes in terms of resources, they also have a broader role; that of government support programmes, such as business incubators and formal entrepreneurial certification schemes. It has been argued in the literature that such programmes serve as credibility signals to outsiders who invest in the program. Incubation and government-sponsored accelerator programmes serve as a way to increase the likelihood of subsequent private investment by lowering the information asymmetry that makes it harder to invest in early-stage companies by certifying that the venture is viable (Isenberg, 2010, 2011; Mason & Brown, 2014). Acs et al. (2017) also support that the institutional environment that surrounds entrepreneurship influences both the quantity and perceived quality of entrepreneurial activity in a region, which in turn impacts the willingness of private investors to invest resources in the region..

Figure 6. The Signalling Function of Government Certification and Incubation Programmes



Source: developed from Isenberg (2010, 2011) and Acs et al. (2017).

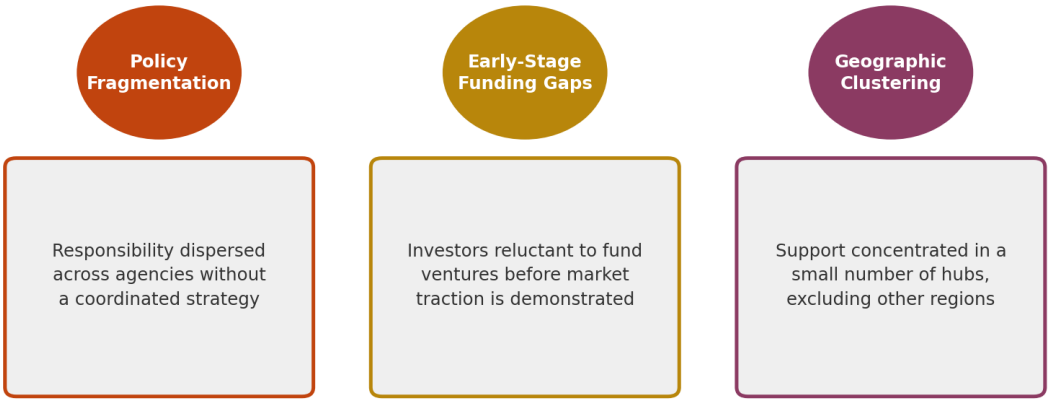
The signalling role is one of the reasons that comparatively small-scale government programmes can have an outsized impact on an ecosystem’s investment climate.

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4.4 Ecosystem Challenges-Fragmentation, Funding Gaps, and Geographic Clustering

While there are positive dynamics, the literature also highlights persistent structural problems that hinder effectiveness of the ecosystem. The first is the fragmentation of the policy area, with entrepreneurship support being addressed by a number of different government departments and their agencies, regional authorities and funding bodies without a coordinated, coherent policy. Fragmentation undermines the coherence identified in the theory of entrepreneurship as essential to productive entrepreneurship (Stam, 2015). First, the lack of early-stage or "seed" funding continued to be a problem in relatively rich ecosystems; and investors were often hesitant to invest in company pre-MVC, especially in the absence of proven market traction, leaving many promising startups undercapitalized early (Mason & Brown, 2014). Third, entrepreneurial ecosystems tend to be spatially concentrated, meaning they cluster in a handful of urban areas that possess the concentration of talent, capital and institutions necessary to facilitate productive entrepreneurship (Audretsch & Belitski, 2017; Malecki, 2018).

Figure 3. Structural Challenges Facing Entrepreneurial Ecosystems



Source: synthesised from Stam (2015); Mason & Brown (2014); Audretsch & Belitski (2017); Malecki (2018).

This is a natural agglomeration, but at the same time may limit the access of entrepreneurs outside these hubs to networks and resources that help to develop and grow ventures, making for questions of inclusiveness and regional balance over time in the implementation of ecosystem-based development strategies.

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5. Growth of collaborative and sustainable ecosystems

Based on the results presented above, it is clear that a sustainable growth in an entrepreneurial ecosystem does not simply happen in response to any single intervention, but only as the result of coordinated efforts of many actors each providing a different capacity. Human capacity – the accumulated experience, mentorship, and technical skill provided by universities, experienced entrepreneurs, and professional networks and institutional capacity – incubators, accelerators and regulatory bodies that can make policy intent into accessible support services must match financial capacity contributed by venture investors, banks, and public funding bodies.

In this regard, Cohen's (2006) sustainable-ecosystem model is helpful: he claims that a true sustainable entrepreneurial ecosystem does not just emerge through a collection of individual support programmes, but must be intentionally brought together through the deliberate alignment of formal and informal networks, physical infrastructure and local culture. For the current results, it means that ecosystem builders need to focus on the quality of coordination in the financial, human, and institutional dimensions. Instead of adding more of any given resource in isolation, for instance, by incorporating mentorship into an incubation programme, or by tying government certification schemes straight to investor networks.

This cooperative model is strengthened by a favourable regulatory environment that reduces transactional costs of establishing new ventures, safeguards intellectual property and sets forth consistent investment exit procedures. As pointed out by Acs et al. (2017), the institutional origins of the ecosystem approach include the understanding that formal rules and informal norms are co-evolving; regulatory reform, therefore, is unlikely to be effective without efforts to foster local entrepreneurial culture and network. Resilience of the connective tissue is crucial to sustainable growth in this sense: it is the ability of capital providers, knowledge institutions, government bodies, and the entrepreneurs themselves to be resilient.

6. Policy and Institutional implications

The reviews of the evidence have a number of implications for policy and institutional actors aiming to make entrepreneurial ecosystems more dynamic. First, coordination mechanisms like a single lead agency or cross-agency task force should be set up to limit the policy fragmentation that

was identified as a common constraint to facilitate the creation of finance, incubation, education and regulatory reform programs as complementary elements of a coordinated strategy, rather than programs in isolation (Stam, 2015). Second, certain instruments need to be developed to fill the funding gaps at the early stages, such as matched public-private seed funds or guarantee schemes to mitigate risk for private investors in pre-traction ventures (Mason & Brown, 2014). Third, in the case of ecosystems, policy makers in secondary regions should seek to make deliberate efforts to link local entrepreneurs to existing ecosystems through satellite incubators, virtual mentorship programs, or regional university collaborations—or some combination of these approaches rather than trying to create a full-strength version of that ecosystem locally (Audretsch and Belitski, 2017).

Finally, government certification and incubation programmes should be explicitly developed to serve their signalling purpose and the criteria for certification should be sufficiently strict to signal to investors that they have a high level of confidence in the information being provided, thereby giving public investments a leverage effect of relatively limited public resources (Isenberg, 2011; Acs et al., 2017).

7. Future Directions

The findings of this evidence review have a few implications for policy and institutional stakeholders aiming to develop entrepreneurial ecosystems. First, coordination mechanisms that minimize the policy fragmentation found in the survey (which is a recurring constraint) will need to be designed, such as a single lead agency or the cross-agency task force, with all finance, incubation, education, and regulatory reform initiatives being part of a more unified strategy rather than standalone programmes (Stam, 2015). Second, there is a need for targeted instruments to address the early-stage funding shortfall, such as matched public–private seed funds, or guarantee schemes that cut the risk associated to private investors in pre-traction ventures (Mason & Brown, 2014).

Third, respecting the geographical density of some ecosystems, some policy initiatives in other areas should focus on deliberate efforts to link local entrepreneurs with known ecosystems via satellite incubators, virtual mentorship networks or regional university arrangements, instead of trying to replicate the full concentration of a major ecosystem in another city (Audretsch & Belitski, 2017).

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Lastly, government certification and incubation programmes should be intentionally tailored to their signalling role, with clear, strong certification criteria that provide investors with reliable information, and should seek to maximize the leverage effect of the relatively small number of public resources (Isenberg, 2011; Acs et al., 2017).

8. Conclusion

This paper synthesised empirical and theoretical work from the literature on entrepreneurship to explore the impacts of entrepreneurial ecosystems on the development and longevity of the start-ups and SMEs. The evidence suggests that no single ecosystem component works on its own, but that capital availability interacts with the quality of mentorship, institutional support from universities and market actors can enhance the value creation potential of SMEs, and government programmes can have a greater signalling effect than delivering resources themselves. Concurrently, ecosystems continue to be held back by policy fragmentation, early-stage funding gaps, and geographic concentration, which ultimately affect the inclusiveness of entrepreneurship-led development.

This is a challenge that needs to be solved through a package of measures that are coordinated across all financial, human and institutional dimensions within a conducive policy-legal environment rather than being pursued as three policy areas. Both scholars and policymakers take away the important message that the power of an entrepreneurial ecosystem is in the relationship between its constituent parts.

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