Second-Tier Stock Markets: The Hidden Engine Behind Global Entrepreneurship

Forthcoming at Management Science

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Many countries established their second-tier stock exchanges following the idea and format of NASDAQ in order to promote entrepreneurship and high-tech startups. These specialized trading platforms, designed specifically for young, innovative companies that cannot meet the stringent requirements of main stock exchanges (such as NYSE), have emerged as an important catalyst for global entrepreneurship. Unlike traditional main stock exchanges that demand lengthy operating histories, proven profitability, and substantial tangible assets, second-tier markets welcome companies with innovative business models, growth potential, and intellectual property-based value propositions – all of these features constitute intermediary platforms between private venture funding and full public market listing.

In this paper, we empirically examine the role of these second-tier stock exchanges in fostering entrepreneurship from a global perspective. We construct a comprehensive country-industry-year panel of venture capital-invested startups across 159 countries from 1990 to 2020. Our analysis reveals a significant 47% increase in entrepreneurial activity following the launch of these specialized exchanges. The launches of 101 new second-tier exchanges in 55 countries during our study period provides were associated with improved exit opportunities on startup creation and innovation, demonstrating how capital market infrastructure directly influences real economic outcomes. We have implemented several identification tests to support a causal interpretation of such a relation.

The mechanism underlying this entrepreneurial boom centers on the resolution of a critical market failure in traditional capital markets. Before the advent of second-tier exchanges, innovative startups face a challenging financing environment where venture capital (VC) is the primary source of growth capital, but exit opportunities for VC remain severely constrained due to the high standard of being listed in main stock exchanges. Our evidence suggests that when VCs can more readily envision successful exits through public offerings through second-tier exchanges, they increase both the volume and size of their investments in startups while offering more favorable terms to entrepreneurs.

Additional analysis shows that startups founded after the establishment of second-tier markets demonstrate increased patenting activity and receive higher valuations from both private and public investors, suggesting that improved access to public markets enhances not just the quantity but also the quality of entrepreneurship. These results mitigate concerns that second-tier markets might attract lower-quality companies seeking to avoid rigorous listing standards.

The impact of second-tier exchanges varies significantly across different economic environments, with the strongest effects observed in countries that combine these specialized markets with complementary institutional features. Nations with strong intellectual property protection, high-quality human capital, robust rule of law, lower unemployment rates, and abundant money supply experience the most pronounced increases in entrepreneurial activity following second-tier market launches. This heterogeneity suggests that while second-tier exchanges represent a necessary condition for enhanced entrepreneurship, they work most effectively when embedded within broader ecosystems that support innovation and business development.

Overall, our evidence shows that second-tier stock exchanges represent a market-based solution to the challenge of translating scientific and technological advances into commercial ventures. By providing clearer pathways from startup to successful exit, these exchanges help countries build more vibrant entrepreneurial ecosystems that can compete effectively in the global innovation economy. Our study contributes to the broader literature on entrepreneurship and economic development by showing how institutional changes in capital markets can have far-reaching effects on innovation activity, offering policymakers a powerful tool for enhancing their countries' entrepreneurial capabilities through market mechanisms rather than direct government intervention.

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