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Incentivizing Innovative Entrepreneurship in Quasi-Markets: Theory and Evidence from Sweden's Schools and Nursing Homes

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Abstract. This article discusses welfare quasi-markets, a promising yet under-explored area of study in entrepreneurship research. Many countries have implemented quasi-markets to enhance entrepreneurship and innovation in welfare service provision. However, the benefits have often been limited, as Sweden's experience illustrates. Based on the Swedish experience, we contend that quasi-markets can unlock their innovation potential only under a suitable institutional framework. By analyzing the development of quasi-markets in primary and secondary education and elderly care nursing homes, we demonstrate that competition and profit incentives, though crucial, are insufficient catalysts for sustained innovation in quasi-market contexts. Such markets require epistemically supportive institutions. These institutions should enable users to make knowledgeable choices and motivate entrepreneurial providers to compete and innovate in ways that align with user preferences.

Keywords: Entrepreneurship; Innovation; Quasi-markets; Welfare services; Schools; Nursing homes.

JEL Codes: H42, H44, H75, I22, I28, L88, O31.

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1. Introduction

The entrepreneurship literature highlights the critical role of institutions in shaping economic behavior (Baumol, 1990; Davidsson & Henrekson, 2002; Henrekson, 2007; Bjørnskov & Foss, 2013; Minniti & Lévesque, 2008; Bylund & McCaffrey, 2017). Yet, it has paid little attention to quasi-markets—an increasingly prevalent institutional phenomenon where public services such as education and healthcare are delivered by competing providers, both public and private, under government funding (Ferlie, 1992; Le Grand, 2009). Despite the global growth of quasi-markets (Le Grand, 2009; Blix & Jordahl, 2021), few entrepreneurship studies address how these markets incentivize entrepreneurial behavior and innovation.¹ This paper seeks to fill that gap.

In quasi-markets, the state “is to become primarily a funder, purchasing services from a variety of private, public and voluntary providers, in competition with each other” (Ferlie, 1992, p. 81). Such markets were introduced to inject competition, efficiency, and innovation into welfare services without compromising user equality (Hood, 1991). It seems evident that entrepreneurship scholars can offer valuable insights into how these markets function. Specifically, quasi-markets relate to key entrepreneurial concepts: opportunity alertness (Kirzner, 1973; McMullen et al., 2007), ownership and judgment (Knight, 1921; Foss & Klein, 2015), and innovation (Schumpeter, 1934; Malerba & McKelvey, 2020), all within an institutional framework (Baumol, 1990).

Three reasons make quasi-markets particularly relevant for entrepreneurship research. First, their sheer size presents significant entrepreneurial opportunities (Kirzner, 1973). For example, government spending on welfare services constitutes about 15% of GDP in several OECD countries (*Table 1*), and in Sweden, private providers account for between 16% and 49% of service provision (*Table 2*). Second, the presence of private firms underscores the role of ownership and resource control (Knight, 1921; Foss & Klein, 2015). However, quasi-market rules—such as procurement contracts—often restrict entrepreneurial autonomy, limiting

¹ *Small Business Economics* is no exception in this regard; while many articles, e.g., discuss general conditions for entrepreneurship and firm growth, we have been unable to find any articles that explicitly focus on the welfare sector or quasi-markets. Relevant results are also scant in the management literature, even though Ferlie (1992) identified quasi-markets as an important research topic for strategic management more than 30 years ago. That said, management scholars have made important contributions such as the potential advantage of for-profit firms in advancing social welfare (Besley and Ghatak, 2001; Luo and Kaul, 2019), the importance of public-private hybrid governance forms and alliances to generate desirable outcomes (Rangan et al., 2006; Cabral et al., 2013), and the strengths of different organizational forms in different contexts (Quélin et al., 2017; Luo and Kaul, 2019). One study that may appear to be directly related to ours is Boettke et al. (2011), who discuss quasi-market failure. However, they discuss a polycentric system that permits multiple, competing, lower-level governmental jurisdictions in urban settings. This is very different from the kinds of quasi-markets we analyze.

incentives for productive use of resources. Understanding and overcoming such challenges is likely paramount for increased innovation in these sectors. Third, welfare services in many countries face mounting financial pressures, as spending trends are unsustainable (OECD, 2021). Innovation is vital to enhancing productivity and alleviating financing pressure (Bloom et al., 2019; Torfing & Triantafyllou, 2016), yet existing research offers little guidance on how quasi-market institutions can foster continuous innovation.

Table 1 Government spending on education, health care, and elderly care as a percentage of GDP in selected OECD countries, latest available year.

Country	Child-care	Primary school	Secondary school	Tertiary education	Health care	Elderly care	Total
Canada	0.23	1.97	1.22	1.2	8.70	1.50	14.82
France	1.32	1.14	2.19	1.1	10.34	0.39	16.48
Japan	0.69	1.12	1.28	0.5	9.28	1.85	14.72
Netherlands	0.64	1.14	1.82	1.1	9.47	0.83	15.00
Sweden	1.58	1.94	1.97	1.3	9.79	2.53	19.11
UK	0.56	1.64	1.78	0.5	9.90	0.31	14.69
U.S.	0.32	1.52	1.69	0.9	8.50	0.01	12.94
Average	0.76	1.49	1.71	0.94	9.42	1.06	15.39

Source: OECD.

Table 2 Share of government-financed services produced by private providers, Sweden, latest available year.

Service	Year	Share (%)
Primary school	2025/26	16.4
Secondary school	2025/26	31.5
Primary care centers operated by private providers	2024	49.0
Home help services for elderly	2024	16.1
Nursing homes for elderly*	2024	21.0
Purchases from private firms by regional and municipal authorities as a share of total spending	2024	13.1

* We have replaced the National Board of Health and Welfare's (2022) term "special housing for elderly" with the more familiar term "nursing homes" throughout.

Source: Statistics Sweden, Swedish National Agency for Education, and Swedish Association of Private Care Providers (2026).

Importantly, the design of quasi-market rules has profound allocative effects (Baumol, 1990). If incentives are misaligned, profit-seeking behavior may undermine welfare objectives. Achieving continuous innovation requires not just competition and private sector involvement but also a regulatory framework that aligns entrepreneurial incentives with social goals (Williamson, 2000; Klein et al., 2010). Here, again, entrepreneurship scholars should have plenty to say.

This paper focuses on how policymakers can shape quasi-market institutions to promote value-enhancing innovative entrepreneurship.² We illustrate how policy can strengthen innovation incentives in quasi-markets by drawing on our knowledge of the Swedish quasi-markets in elderly care and schooling. That Swedish entrepreneurs have recognized these sectors as a source of entrepreneurial opportunity is evident (Table 2).³ At the same time, research to date suggests that the overall qualitative and innovative gains from the establishment of these quasi-markets have been relatively modest.

Drawing on Sweden's experience in schools and nursing homes for the elderly, we argue that two conditions are necessary but not sufficient: (1) sustained competitive pressure and (2) a sizable presence of for-profit providers.⁴ We argue that these conditions are central to sustaining long-term innovative pressures in quasi-market models that rely on entrepreneurial entry and replication.

Beyond these necessary conditions, we argue that quasi-markets must address epistemic challenges that limit both user choice and provider innovation (Haeffele & Storr, 2019). A reading of the vast literature on quasi-markets in various sectors suggests that the most common problem in such markets is that users and providers are often in a disadvantaged epistemic position compared with actors in ordinary markets (Haeffele & Storr, 2019). Unless institutions are put in place that produce, validate, and transmit decision-relevant information to users, providers, regulators, and entrants, the beneficial effects one can expect from competition and the presence of for-profit providers are reduced.

An epistemically conducive system is better at creating the kind of information actors need to make sense of the world, better at providing them with this information, and better at generating the incentives they need to construct the knowledge necessary for action.

We contend that institutions should improve the epistemic position of users and providers by:

² For a broader purely theoretical companion paper, see Elert and Henrekson (2026).

³ In fact, Sweden stands out for its considerable presence of for-profit actors in welfare quasi-markets in general, whereas many other countries prohibit for-profit actors in these markets. That said, countries that do allow them, e.g., the Netherlands and Australia, have seen a sizeable increase in the number of for-profit actors in recent years (Karlson & Lundbäck, 2022).

⁴ Entrepreneurship scholars recognize the crucial importance of profits for innovation. Knight (1921) saw profits as the entrepreneur's compensation for investing in innovations characterized by financial uncertainty. Schumpeter (1934, p. 154) observed that "(w)ithout development there is no profit, without profit no development." As we shall see, modern scholars also argue that the profit motive stimulates innovation and better service quality, although it may also have adverse consequences (Shleifer, 1998).

1. Expanding freedom of choice, especially in elderly care, to empower users and create larger, more contestable markets.
2. Enhancing information quality and evaluation criteria, particularly in schools, to ensure that competition focuses on knowledge outcomes rather than superficial indicators.
3. Managing market exits to minimize harm and allow high-performing providers to take over underperforming services.

Our contribution is threefold. First, we bring quasi-markets into entrepreneurship research, highlighting their institutional relevance. Second, we explain why competition and profit incentives are insufficient in welfare quasi-markets. Third, we offer concrete policy recommendations for enhancing innovation capacity through epistemic reforms, notably by identifying epistemically conducive institutions as a design principle for innovation-oriented quasi-markets.

2. Institutional and theoretical background

Klein et al. (2010, p. 5) emphasize that “any change in the institutional environment brought about by public-sector entrepreneurship changes the setting in which private-sector (and public-sector) entrepreneurship takes place” (cf. Ostrom, 1990). Quasi-markets, as institutional creations, are prime examples of this dynamic but remain underexplored in entrepreneurship research. Traditional economic analyses often treat their structure as fixed rather than malleable (Shleifer, 1998; Cabral et al., 2013). However, quasi-markets are not binary choices between public and private provision but hybrid systems whose effectiveness hinges on institutional details.

2.1. Two quasi-market models

Sweden’s quasi-markets emerged from both top-down policy and bottom-up entrepreneurial initiatives (Elert & Henrekson, 2017), particularly in preschools and elderly care (Blix & Jordahl, 2021).⁵ Two main models dominate: the *contracting model* and the *freedom of choice model*.

⁵ In the mid-1980s, a major political confrontation arose regarding the existence of tax-funded private preschools, centered around the establishment of the private preschool company Förskolan Pysslingen AB. The long-standing dispute ultimately led to free entry in childcare provision in 1991, and freedom of choice in the school sector likely would not have happened if not for this regulatory battle. Moreover, before Danderyd’s municipality hired a private contractor in 1989, the existing interpretation of the law was that municipalities had a monopoly on the provision of (fully or partly) tax-financed elderly care. The Court of Appeals ruled that what Danderyd did was not illegal, which paved the way for the subsequent privatization of elderly care (Bergman & Jordahl, 2014).

The contracting model, prevalent in elderly care and other welfare areas, involves procurement where private or public providers bid to run services. Winners receive temporary monopolies, introducing competition *for* the market. Private management is incentivized by profits but risks cutting hard-to-monitor quality aspects (Shleifer, 1998). Strong regulatory oversight is thus needed but may inadvertently stifle innovation.

The *freedom of choice model*, used in schools, preschools, and primary care, fosters competition *within* the market. Users carry publicly funded vouchers, choosing between public, for-profit, or non-profit providers. Competition encourages improvement, as providers risk losing users (Le Grand, 2009). This model arguably tempers profit motives by aligning them more closely with user preferences.

From an institutional lens, designing quasi-markets is a form of public entrepreneurship (Klein et al., 2010). Whether these markets foster continuous innovation depends not only on competition and ownership but also on complementary institutions, particularly those addressing epistemic challenges, the issue to which we now turn.

2.2. Standard economics: necessary conditions for innovation in quasi-markets

Shleifer (1998), drawing on Hart et al. (1997), outlines when private provision is preferable, focusing on *contractibility*—the ability to specify and enforce service quality. Where contractibility is low (as in elderly care), private providers may cut quality to reduce costs. However, three factors mitigate this risk:

1. Importance of innovation: When innovation is vital, private ownership's stronger incentives favor innovation despite quality risks. Yet, it is an open question whether sectors such as elderly care are breeding grounds for innovation. The answer depends on the form of ownership (Klein et al., 2010) and on details in the model used, not least what kind of information the parties involved—providers, clients, and regulators—have access to.
2. Freedom of choice: User choice disciplines providers, aligning incentives. Here, Shleifer's reasoning meets that of Le Grand (2009), who, based on his experience as a practitioner and researcher, argues that (p. 14) “in most situations, services whose delivery systems incorporate substantial elements of choice and competition have the best prospect of delivering a good local service.” The key difference compared to a regular market is that a publicly funded voucher equalizes purchasing power across users.

3. Reputation mechanisms: Providers safeguard quality to maintain reputation, especially when switching costs are low. To be sure, this epistemic dimension can also be influenced, e.g., by introducing a rating system modeled on those used for hotels, taxi services, and subletting.

Shleifer (1998, p. 140) argues that at least one of these conditions usually holds, which means that the normative argument for public production is generally weak. One does not have to fully buy into this conclusion to (i) acknowledge the epistemic line running through each criterion for successful welfare production under private for-profit management, and (ii) acknowledge that no criterion is written in stone. Instead, it seems highly plausible that policymakers can influence a particular quasi-market's epistemic capacity by introducing complementary institutions that are information- and knowledge-conducive. But before we dig into the details of how specific quasi-markets should be reshaped to this effect, it is useful to complement Shleifer's and Le Grand's perspectives with a more evolutionary view.

2.3. The epistemic problem

Certain conditions must be met for quasi-markets to function well. One way to understand whether these conditions are met is to apply an evolutionary perspective to quasi-markets, comparing them to regular markets, where the importance of competition and profit-seeking is evident in the *generation*, *selection*, and *replication* of innovations. In addition, there is a *specification* problem in quasi-markets that has no real equivalent in a regular market.

In free markets, *entrepreneurial rents*—profits exceeding normal returns—reward innovation and constitute the selection criterion (Knight, 1921; Henrekson & Stenkula, 2017). This is evident from a perspective associating entrepreneurship with profit-oriented ownership following Knight (1921), according to whom the pursuit of profit is entrepreneurs' major motivation in introducing innovations and that they can only exercise such entrepreneurial judgment when they own productive resources.⁶

Profits attract competitors, diffusing knowledge and eroding initial profits (Baumol, 2010). Ultimately, consumers benefit through lower prices and better quality (Nordhaus, 2005). Profit signals thus play a crucial epistemic role. For quasi-markets to have innovation potential, the transformation process driven by the existence and creation of entrepreneurial rents is likely

⁶ In contrast to Schumpeter, Knightian scholars argue that entrepreneurship *presupposes* ownership of a business firm, modeling “entrepreneurs as owning, controlling, and combining heterogeneous assets ... and deploying these assets within a firm to produce goods and services in anticipation of economic profit” (Foss & Klein, 2015, p. 585; cf. McMullen, 2015).

crucial. Because government providers with weaker innovation incentives still dominate most welfare sectors, it is critical that existing private providers in these sectors are willing to act entrepreneurially, i.e., to bear uncertainty and innovate in the hope of future returns. Yet, the profit motive is far from uncomplicated in quasi-markets.

Quasi-markets are conservative Most regular product and distribution markets are virtually unrecognizable compared to just a few decades ago. No bureaucrat could have anticipated the way in which they would change. However, because quasi-markets deal with taxpayer money, a principal/bureaucrat who wants to safeguard quality and taxpayer funds must define acceptable services in advance, constraining discovery of unforeseen innovations. This necessity makes quasi-markets inherently more conservative.

Quasi-markets often rely on fixed prices Quasi-markets typically operate under *fixed prices*, ensuring equal purchasing power (Le Grand, 2009). However, fixed prices blunt price signals essential for coordination (Hayek, 1945), limiting providers' ability to signal quality and hampering resource allocation. Queues may partially substitute, but the epistemic disadvantage remains. As Haeffele and Storr (2019) put it, "entrepreneurs in an unhampered market enjoy a privileged epistemic position compared to actors in non-market settings."

Quasi-market actors have different objectives Provider diversity adds complexity. For-profit firms are responsive to demand shifts, expanding when user numbers rise. Non-profits and public entities may lack comparable incentives or financial flexibility, weakening the replication mechanism crucial for innovation dissemination. Granted, non-profits may still diffuse knowledge through example, while competition forces government-run providers to improve (Mahoney et al., 2009; Haeffele & Storr, 2019). However, the fact that most providers in quasi-markets are not driven by profit motives may limit the markets' overall effectiveness.

Quasi-market choice is difficult Freedom of choice models reduce epistemic disadvantages but present challenges. For example, users may lack full information, or others (guardians, relatives) make decisions on their behalf. High switching costs further limit effective competition. The costs (mainly non-monetary) of changing providers are also high, underlining the need for a system that generates the kind of information users need to reduce the risk of making a bad choice.

2.4. In summary

For quasi-markets to foster innovation, they must enable entrepreneurial actors to bear uncertainty and reap rewards. Yet the inherent epistemic challenges—related to service

specification, price signals, and provider motivations—constrain this potential. Policymakers can mitigate these constraints by introducing institutions that enhance information flows and align incentives without undermining competition. Our analysis now turns to how this can be done in practice.

3. Illustrative evidence: two Swedish quasi-markets

Opening a previously closed market to private options can have two potential quality effects: (i) a direct effect resulting from some modes of operations delivering better services than others, and (ii) an indirect effect where the increased competition causes all or most providers to improve. Moreover, the competitive effect can work differently depending on whether providers are chosen through public procurement, user choice, or a combination of the two modes. To get an idea of the extent to which these two effects are at play, we examine the Swedish quasi-markets for elderly care and schooling. When these effects are not present or appear muted, we ask whether they *could be strengthened* by improving the rules of the game. Although both schools and nursing homes are merit goods with information asymmetries and high political salience, they are good contrasting cases. Schools approximate a freedom-of-choice model while nursing homes rely more on procurement;

3.1. Swedish nursing homes in an international perspective: quality and innovation

Surveys of the international literature show that for-profit nursing homes generally perform worse in terms of quality than private non-profits and government providers (Comondore et al., 2009; Xu et al., 2013; Bos et al., 2017). For-profit contractors also seem to do worse in terms of employee satisfaction but better in terms of cost efficiency (Bos et al., 2017). A survey by Tran et al. (2019) reports partly contrasting results, namely that large for-profit nursing homes are more efficient than non-profit counterparts. Regarding the competition effect, Yang et al. (2022) find mixed results when reviewing the international evidence on how prices and quality are affected by competition among nursing homes. However, most studies find that greater competition results in lower prices. Among institutional factors likely to contribute to the unclear picture, the authors highlight an information problem; if relevant information is easily accessible and reliable, they suggest, nursing home competition will more likely have favorable effects, which suggests that the establishment of epistemically conducive institutions may be critical in this welfare sector as well.

The Swedish evidence is less negative. Private providers do worse in terms of structural quality (e.g., staffing level and housing standard) but better in terms of process quality (such as user participation in the development of care plans) (Stolt et al., 2011; Winblad et al., 2017).

Bergman and Jordahl (2014, p. 50) even argue that private providers outperform public providers in most quality dimensions that they can reasonably influence. Broms et al. (2020) differentiate between the direct and indirect effect and find that, on average, Swedish private nursing homes provide services of comparable quality to public providers.

In their review, Yang et al. (2022) point out that competition plays a limited role in Sweden because the procurement model dominates so strongly. Nevertheless, Bergman et al. (2016) show that nursing home mortality (a highly relevant measure of non-contractible quality) is lower in municipalities where the market has been opened for private actors (they make no distinction between procurement and freedom of choice). The authors attribute the beneficial effect to a combination of private ownership and competition for the market. Their conclusion receives some support from Broms et al. (2020), who find that the threat of private competition (measured as the presence of private firms in the market) prompts government providers to improve. Furthermore, they find that staff quality is higher among private nursing homes in municipalities with freedom-of-choice competition. However, they find little evidence that greater competition for the market (measured as more tenders) would lead to higher quality.

A cautious interpretation of the results is that the establishment of quasi-markets for nursing homes in Sweden has been successful in an international perspective. Blix and Jordahl (2021, p. 114) reach a similar conclusion when summarizing the evidence concerning the Swedish elderly care reforms:

... it seems that privatized elderly care has distinct cost advantages. Some quality improvements are also observed with privatization: reduced mortality rates and better process quality measures in nursing homes. Public nursing homes on their part have an advantage on structural quality measures, although this is less evident than the private advantage in process quality measures.

As regards innovations, there is considerable potential for cost savings and quality and safety enhancements if elderly care becomes better at adopting new technology (SOU 2020:14). However, new technology may be a double-edged sword that either strengthens or hampers the co-production between providers and users (Gallouj & Savona, 2009). To date, few studies have investigated preferences regarding the introduction of welfare technology in elderly care, suggesting that a one-sided focus on welfare technology risks missing the target to the point of being counterproductive. The risk increases, for example, if the technology undermines control, independence, and other aspects that users value (Persson & Olofsson, 2022).

However, technology is not the only innovation route; in a systematic review, Brodtkorb et al. (2019) conclude that leadership is key to successful innovations that lead to more patient-focused care in nursing homes. There also appears to be a clear connection between management and organizational form: Angelis and Jordahl (2015) use the interview method developed by Bloom and Van Reenen (2007) to compare management practices in 500 private and publicly owned Swedish nursing homes. They find that the management function is consistently superior in private nursing homes. The authors also find some support for a positive relationship between management quality and care quality, noting that the results align with the international management literature in other areas (Angelis & Jordahl, 2014).

3.2. Swedish schools in an international comparison: quality and innovation

The international evidence suggests pupils' school results benefit from quasi-market reforms (Shakeel et al., 2021; Cohodes & Parham, 2021) and that the beneficial effects occur both because private providers do well (Chabrier et al., 2016) and because competition encourages all providers to improve (Figlio et al., 2023). In view of these facts, it is noteworthy that international tests show that the Swedish school system experienced a severe decline in knowledge combined with grade inflation shortly after the freedom-of-choice reforms of the 1990s (Henrekson & Wennström, 2022). However, the decline appears to have started before the enactment of the quasi-market reforms (Holmlund et al., 2014), and the school system changed in other ways during the same period. In addition to the free school reform, Holmlund (2020) lists decentralization, new curricula, new grading systems, changed teacher training, stricter entrance requirements to upper secondary school, digitalization, and a plethora of government support programs for principals. For this reason, Holmlund (2020, p. 6) notes that it is, in principle, "impossible to sort out the reasons behind the fall and rise of Swedish students in the PISA study. Too many changes have been implemented more or less simultaneously for it to be possible to isolate direct causal relationships."

Blix and Jordahl (2021, pp. 135–136) nevertheless venture a cautious interpretation, summarizing the effects of the Swedish school quasi-market as follows:

[T]he introduction of independent schools has increased the productivity of the Swedish school system. This is evident for the compulsory level (with students aged 6 to 15) where competition from independent schools has raised student performance without raising costs. ... At the upper-secondary level, the evidence is more mixed. Students at independent schools have higher grades and test results and are more likely to graduate on time and to continue to tertiary education. However, when comparing internally and externally graded tests, students of independent upper-secondary schools actually perform worse but benefit

more from lenient grading. ... Finally, it should be stressed that the gains from competition have been relatively modest in size and have not prevented the decline in the PISA ranking.

In Blix and Jordahl's (2021) assessment, the free school reforms probably did not contribute to the Swedish knowledge decline. There is also little to indicate that outcomes would have been noticeably better if all the changes that Holmlund (2020) enumerates had taken place except for the free school reform. Indeed, things could have been worse without this reform, as suggested by the poor student results in those areas of the country where parents have low education and the school remains a de facto local monopoly because there has been no entry of independent schools (Heller Sahlgren, 2021).⁷ Still, it seems clear that any gains from the Swedish school marketization have, at best, been modest. This lack of progress is noteworthy given that no other country has marketized children's education so systematically and to the same extent (Blomqvist, 2004; Wennström, 2020). If competition and high-powered incentives were sufficient to the provision of education, one would expect Sweden to have seen more consistent and continuous benefits than any other country, yet this has been far from the case.

The impetus behind greater technology use in the classroom is that technology could advance student learning by enabling more hours of high-quality, individualized learning (Chatterji, 2018). Unfortunately, the scant evidence on technological classroom innovations that lead to knowledge-enhancing outcomes is not encouraging (Bulman & Fairlie, 2016). In a Swedish study, Hall et al. (2021) examine the effects of a so-called 1:1-program aiming to make information and communication technology an essential part of education in all subjects. The only demonstrable effects are deeply problematic: 1:1-programs risk increasing school inequality by *worsening* math skills and future admission prospects for students with low-educated parents. On the other hand, the use of so-called CAL (computer-assisted learning) software can be compatible with sizeable positive learning effects, though they are expensive (Biasi et al., 2022, p. 12). The mixed results highlight the fact that a key characteristic of service production and service innovations is that they are co-produced (Aligica et al., 2019, Ch. 6; Ostrom & Ostrom, 1991), by teachers and students in the case of schools. New technology can strengthen that co-production but may also undermine it. This risk appears particularly high for low-performing students. These facts should encourage caution but also sound evaluation strategies—one example is Chatterji and Jones' (2016) EDUSTAR platform, which quickly evaluates digital learning activities in the classroom using randomized experiments. Rapid

⁷ Heller Sahlgren (2023) finds that increased local competition has improved TIMSS scores, which is driven by for-profit schools. A simulation based on the estimates indicates that Sweden's average score in TIMSS 2019 would have been 0.24 standard deviations lower without the expansion of the independent-school sector.

evaluations of software and hardware could result in a safer introduction of knowledge-enhancing technology.

However, new technology is only one type of innovation. An earlier review of the international evidence on school quasi-markets and innovations finds that they primarily promote management and marketing innovations (Lubienski, 2009, p. 43). In his more recent overview, Chatterji (2018) also discusses the great potential of organizational innovations and the extensive literature on new forms of organization and management in schools. That these kinds of innovations are significant is confirmed by international evidence on the connection between management/school governance and educational results (Bloom et al., 2015). The study covers eight countries, including Sweden, and the association is strongly positive: better school management has a considerably stronger association with school results than do factors such as teacher density and class size. The link was also strongest in England, where the most reliable measures of educational quality are available, but weaker in Sweden, where student grades are unreliable quality measures. Other studies confirm the connection between better school management and good educational outcomes (e.g., Dobbie & Fryer, 2013; Angrist et al., 2012; Bloom et al., 2015). Fryer (2017) also shows that management training of principals has a causal, positive effect on student learning.

Moreover, Bloom et al. (2015) show that half the variation in management quality is at the country level—significantly higher than in similar studies by the same researchers regarding other parts of the economy. Publicly funded independent schools also have a significantly better management function than public schools and fully private alternatives. Bloom et al. (2015, p. 2) conclude that “differences in the institutional environment have particularly important effects on the way schools are managed.”

4. Epistemic reform proposals: how to make quasi-markets more innovative

As we have argued, quasi-markets’ capacity for innovation hinges not only on competition and ownership but also on the design of complementary institutions. Drawing on theory and empirical insights, we propose three reforms aimed at strengthening the epistemic foundations of Sweden’s school and nursing home quasi-markets. All reforms are relevant to both sectors, although to varying degrees.

4.1. Strengthen the freedom of choice

The entry of private providers in both sectors following the 1990s reforms has introduced competition—but in Swedish nursing homes, the *procurement model* predominates, which is about competition *for* the market while barring competition *within* the market. Providers largely compete for procurement officials’ approval rather than for users. Similarly, in some municipalities, schools function as de facto monopolies due to lack of entry. This weakens both the innovative pressure and the epistemic value of competition.

While there is arguably something akin to an entrepreneurial rent here—the winner of a procurement contract gets a de facto monopoly—this rent cannot be eroded by subsequent imitators because they are effectively blocked from entry until the contract is up for renewal (Henrekson & Stenkula, 2017; Holcombe, 2013). Relatedly, the low degree of actual competition eliminates the epistemic and disciplining effects of continuous competition. In the extreme, a sole provider has no challengers and therefore limited guidance about what users value; there is, therefore, a considerable risk that the provider either focuses efforts along dimensions users do not value or even undertakes cost savings that reduce quality (Shleifer, 1998; Le Grand, 2009).

To address this problem, freedom of choice should be strengthened where it exists (schools) and introduced alongside procurement models (nursing homes). Giving users vouchers that follow them allows entrepreneurial entry and ensures that demand reflects users’ subjective preferences. However, such a system requires markets large enough to make entry viable—suggesting that catchment areas should be expanded, e.g., allowing care allowances to be portable across municipalities. A user in the big city could then choose a nursing home with attractive surroundings in a rural area (where operating costs are lower), but without changing the user’s formal municipality of residence so that the municipality that granted the service pays the care allowance to the provider in the rural municipality. Such an expansion would enhance the opportunities for replicative entrepreneurs. For schools, attempts should also be made to improve competition and user choice in municipalities where this is lacking.⁸

Additionally, private nursing homes often offer supplementary services thanks to household service tax deductions. Extending this right to public providers would allow all actors to experiment and better gauge user preferences, strengthening entrepreneurial incentives. As

⁸ Since the free-school reform, private schools have been established in almost 200 of Sweden’s 290 municipalities, and almost all municipalities have pupils who live there while attending a private school in another municipality (Almega, 2021).

Karlson and Lundbäck (2022) put it when discussing such supplementary services in home care, they can function as “a kind of experimental workshop and a gauge of what the elderly really need help with.” This would greatly strengthen entrepreneurs’ “buy low and sell high” function (Kirzner, 1973) and generally aid entrepreneurs in their profit-driven judgmental decision-making. That said, a policy introducing similar topping-up opportunities in the case of schools is subject to considerable fairness concerns, which are beyond the scope of this paper.

4.2. Improve information and evaluation criteria

Quasi-markets inevitably rely on public specification of service content. However, broad yet concrete specifications are crucial to balance user choice with meaningful competition. Nowhere is this clearer than in Swedish schools. With vague and ill-conceived objectives, the willingness of companies to compete and pursue profit rarely leads to desirable outcomes.

The foremost obstacle to realizing knowledge-enhancing innovation in Swedish schools relates to two institutional changes which coincided with the marketization of schooling in the early 1990s (Holmlund, 2020): a shift to a postmodern view of knowledge, reflected in curricula downplaying objective knowledge, and a grading system that decentralizes grading decisions to individual teachers without external oversight and with no right to appeal. Combined, these developments undermine reliable quality indicators and create incentives to inflate grades rather than improve actual knowledge (Henrekson & Wennström, 2022; Bloom et al., 2015).

A postmodern view of knowledge had been gaining ground for decades and took hold with the 1994 curricula. This view weakened the teacher’s knowledge-transmission role (Henrekson & Wennström, 2022). This is hardly surprising, given that this view of knowledge questions the very existence of objective knowledge and deprives the teacher of the mandate to convey the kind of knowledge students need by insisting that the students should construct this knowledge themselves.⁹ By undermining any claim to a common foundation of knowledge, the postmodern view has created a substantial epistemic obstacle.

Sweden also transitioned from a relative grading system to a goal- and criterion-based one in 1994. The new system meant (at least on paper) that students were not compared with their peers, only assessed based on whether they achieved the learning goals (Nordin et al., 2019).

⁹ According to the view that was replaced—the classical view—traditional subject delineations and fact-based learning are the best way to build the knowledge needed to solve problems, think critically, and develop one’s creativity (Kirschner et al., 2006; Willingham, 2010; Tricot & Sweller, 2014). Thus, creativity, problem-solving, and critical thinking are considered (important) side effects when studying subjects at a successively more advanced level.

At the same time, grading was decentralized to the teachers so that they were allowed to set grades practically without any external oversight (Wennström, 2020). This new design of the grading system made grades unreliable measures of knowledge, resulting in grade inflation and dramatic differences in grades between schools for comparable performance. The grading system thus becomes an obstacle for schools to compete in terms of knowledge. These distorting control measures, in turn, channel the profit motive and competitive incentives in (partly) the wrong direction.

Reforms that improve knowledge beliefs and grading systems that limit grade inflation would create a self-reinforcing effect between trust and control. The epistemic problem would be significantly reduced, which would build sound incentives for knowledge-enhancing innovation into the system of choice. Moreover, the positive consequences would be quickly felt. Such reforms may improve incentives without requiring large additional expenditures—student achievement would improve across the board (Betts & Grogger, 2003; Figlio & Lucas, 2004), as would the potential for knowledge-enhancing innovation in the school market. A joint approach would pave the way for more innovation-driven entrepreneurs and give them greater degrees of freedom in terms of judgmental decision-making, while also empowering users with the necessary knowledge to make informed choices.

In addition, both the school and nursing home markets would benefit from making information from user surveys easily accessible and understandable. Introducing or strengthening reputation mechanisms in both sectors (e.g., rating systems akin to those used in private services) would offer prospective users better decision-making tools and incentivize providers to maintain and improve quality. In procurement contexts, regulators should also allow evaluations based on past performance, reducing the information asymmetry faced by procurement officials and users alike (Lundberg et al., 2022).

4.3. Manage exits to minimize harm and promote learning

The logic of choice in quasi-markets is that providers who do not attract enough users should be financially penalized. Ideally, choice acts as a feedback mechanism that gives weaker providers the opportunity and reason to correct their course. Nevertheless, failures are inevitable in a competitive system, but it is important that users do not suffer needlessly.

First, it may therefore be desirable to minimize the risk of dramatic failures occurring at all, for example, by requiring financial guarantees (e.g., bank guarantees) from operators, ensuring continuity in case of failure while creating incentives for financial prudence. The guarantee

would provide an incentive for another actor, the bank, to monitor the operator's finances and protect users against sudden closure by ensuring that a guaranteed amount is made available to the new operator. This also puts a price tag on the municipality's obligation to ensure without delay that all users in the municipality have a place, improving the epistemic position of present providers, those considering entrepreneurial entry, and the municipal principals.

The failures that do occur should be costly, not for users, but for providers who must bear the consequences of their incompetence. In schooling, one approach would be to grant an agency, such as the Swedish Schools Inspectorate (*Skolinspektionen*), powers to place underperforming schools under compulsory administration, allowing competent external actors to take over rather than defaulting to municipal management. At present, the regulatory framework is such that the municipality itself has to run a school after closure, regardless of how ill-equipped it is to do so. The provider who takes over should also be given greater degrees of freedom in terms of pedagogy and rules of order to remedy a poor educational environment. There is U.S. evidence of beneficial effects when underperforming schools are replaced by a charter school, likely because the takeover often emphasizes discipline and intensive student-focused instruction (tutoring) (Cohodes & Parham, 2021).

These measures ensure that poor performers face consequences, reinforcing entrepreneurial discipline while minimizing user harm. Importantly, they improve the information environment by clarifying the rules and responsibilities around failure, making market conditions more predictable for entrants.

4.4. Implications

Taken together, these reforms would significantly strengthen quasi-markets' innovation potential. By improving information flows, aligning incentives, and managing exits effectively, they would:

- Enhance entrepreneurs' ability to exercise judgment and identify user-valued innovations.
- Empower users with the information necessary to make informed choices.
- Promote continuous improvement while safeguarding service quality and equity.

Ultimately, well-designed quasi-markets hold the promise of delivering cost-efficient, high-quality welfare services, provided their epistemic foundations are sufficiently robust.

5. Conclusion

Private entrepreneurs have an important role to play in quasi-markets for welfare services, but frameworks need to be appropriately designed to realize the full potential of their entry. Nevertheless, some rules governing these quasi-markets will inevitably fall short initially and some of the positive effects of the reforms may be delayed. Add to this the fact that there is public-private entanglement of the systems under discussion. While the public sphere has the capacity to choose the rules of the game, i.e., institute the regulations we propose, government actors also “play the game,” in the sense that government providers are big players in all Swedish welfare markets, making them an important interest group which may favor profit restrictions and other measures that limit competition, including measures that facilitate users’ comparisons of quality (Wagner, 2016).

To ensure that the interests of government providers, profit-seeking firms, and society coincide, policymakers need to safeguard the stability of the system by taking a long-term view and continuing to emphasize the value of competition and for-profit companies while adjusting the regulatory framework in response to weaknesses that transpire. This will also reduce the temptation to exploit weaknesses in the system. Instead, companies can think about their long-term commitment and all providers can focus on developing better welfare services.

The point of the reforms we have proposed is to make it easier for welfare markets to generate the necessary information and knowledge themselves. Providers are then better able to compete based on what users value, which stimulates innovations that, if they prove valuable, are then copied by other providers. Because these markets are still dominated by government providers with weaker incentives to innovate and improve, it becomes even more important that the private providers that do exist can take risks in the hope of future returns. With well-balanced regulations, the private interest of profit can be made to coincide with the interest of society.

This paper contributes to the entrepreneurship literature in several ways. First and foremost, we add considerable concreteness and real-world relevance to the discussion of the relationship between institutional frameworks and the resulting entrepreneurial action, and how activities at the intersection of public and private interests can best be organized, by highlighting the previously overlooked importance of quasi-markets. Additionally, we show how such markets can increase their innovation potential by essentially tailoring complementary institutions that are epistemically conducive, in the broad sense, so that they provide information that helps entrepreneurs make sense of the world and construct knowledge necessary for action. The

importance of such institutions for steering for-profit competition towards desired social goals has hitherto been overlooked.

Like any study, ours has its limitations: the cited evidence is illustrative rather than causal covering two sectors in one country, innovation is difficult to measure directly, and our policy proposals are theoretically grounded but not empirically tested.

Our key motivation has been to shed light on what we see as an underappreciated topic for entrepreneurship scholars, drawing on entrepreneurship theory and two Swedish illustrative examples to underscore why entrepreneurship scholars should care about quasi-markets, and, crucially, demonstrate what scholars in this field can contribute. We hope that future entrepreneurship studies will approach this topic using all the tools in the qualitative and quantitative analytical toolkit.

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Table 1 Government spending on education, health care, and elderly care as a percentage of GDP in selected OECD countries, latest available year.

Country	Child-care	Primary school	Secondary school	Tertiary education	Health care	Elderly care	Total
Canada	0.23	1.97	1.22	1.2	8.70	1.50	14.82
France	1.32	1.14	2.19	1.1	10.34	0.39	16.48
Japan	0.69	1.12	1.28	0.5	9.28	1.85	14.72
Netherlands	0.64	1.14	1.82	1.1	9.47	0.83	15.00
Sweden	1.58	1.94	1.97	1.3	9.79	2.53	19.11
UK	0.56	1.64	1.78	0.5	9.90	0.31	14.69
U.S.	0.32	1.52	1.69	0.9	8.50	0.01	12.94
Average	0.76	1.49	1.71	0.94	9.42	1.06	15.39

Source: OECD.

Table 2 Share of government-financed services produced by private providers, Sweden, latest available year.

Service	Year	Share (%)
Primary school	2025/26	16.4
Secondary school	2025/26	31.5
Primary care centers operated by private providers	2024	49.0
Home help services for elderly	2024	16.1
Nursing homes for elderly ^a	2024	21.0
Purchases from private firms by regional and municipal authorities as a share of total spending	2024	13.1

^aWe have replaced the National Board of Health and Welfare's (2022) term "special housing for elderly" with the more familiar term "nursing homes" throughout.

Source: Statistics Sweden, Swedish National Agency for Education, and Swedish Association of Private Care Providers (2026).