

Resolution Foundation

Just the job – or a working compromise?

*The changing nature of self-
employment in the UK*

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Executive Summary

The growth of self-employment has become one of the stories of the recovery. While the share of total UK employment accounted for by self-employment has risen for decades, bucking the trend internationally, its pace has accelerated since 2008. And while the number of employee jobs has only recently regained its pre-recession level, the number of people who are self-employed has grown by 650,000 since 2008 to reach 4.5 million, or nearly 15 per cent of all employment.

The scale of this increase—and what it means for the self-employed and the wider economy—has sparked much debate. For some, higher self-employment levels are an indication that the recovery is built on shaky ground. There are suspicions that many of the newly self-employed are there unwillingly, forced to go it alone due either to a lack of employee jobs or unscrupulous employers looking to minimise their liabilities. There are also claims that people who may previously have remained unemployed have been encouraged to register as self-employed to access tax credits, but without the skills or desire to do so. Seen through this lens, self-employment represents another kind of precarious work, in the same vein as zero-hours contracts, leaving many with little security and few employment rights.

For others, the uptick in self-employment is regarded in a much more positive light and is held up as one of the success stories of the past few years. Government support to help people become self-employed, through schemes like the New Enterprise Allowance, is seen as having complemented a long-term structural change in the UK labour market. This change has manifested itself as more entrepreneurs making the shift towards the relative freedom of working for yourself, and a trend towards “portfolio careers” and freelancing.

Our analysis of national datasets and a new survey of just under 1,000 self-employed people suggests that both structural and cyclical elements are at play in explaining the rise in self-employment. There is strong evidence of a **significant structural element**:

- The number of people in self-employment, and particularly its share of total employment, has risen steadily since the early-2000s, pre-dating the downturn.
- The majority of the changes we have seen in the characteristics of the total population of self-employed people and those entering self-employment—better educated, increasingly working in service sectors—are mirrored in changes among employees. Aside from these whole-workforce trends, the self-employed do not look significantly different to before the recession; there are just more of them.
- Closer analysis of the trends in people entering and leaving self-employment prior to the recession and following it shows that 28 per cent of the overall growth in self-employment is due to a decline in the rate at which people leave self-employment. Our view is that this is partly explained by the UK’s expanding and ageing workforce. The raising of the retirement age, longer life expectancy and low levels of pension saving may have led to people remaining in employment for longer, and because self-employed people tend to be older than employees, this disproportionately affects this group. Self-employment might be growing as an alternative or complement to retirement, rather than as an alternative to being an employee.

- A survey conducted by Ipsos MORI for the Resolution Foundation confirms that the majority (73 per cent) of people who became self-employed since the recession did so wholly or partly due to their personal preference for this way of working, and not solely due to a lack of better work alternatives.
- Changes in the nature of self-employment—freelancing rather than owning a business, ‘one-man bands’, and combining self-employment with working as an employee—were evident before the downturn and do not appear to have been particularly affected by it.

While structural trends seem to dominate, there does also appear to be **an important cyclical component** contributing to recent self-employment growth:

- The proportion of the self-employed who work part-time has risen from 23 per cent to 28 per cent since 2005, which is twice as large as the shift among employees. This is complemented by evidence that underemployment is somewhat higher among self-employed people than employees.
- There has been a shift in the destinations of unemployed people who move into work: prior to the recession 8 per cent moved into self-employment, whereas in the post-recession period the figure was 11 per cent. We estimate that this shift explains up to 24 per cent of the overall growth in self-employment. Although some of this may be structural—reflecting changing routes into work and the incentives of recent policy changes such as the New Enterprise Allowance—it is reasonable to conclude that in large part it reflects cyclical factors such as low employee vacancy levels and high competition for available jobs in the post-recession period.
- Although self-employment has grown in most regions of the UK in the years since the recession, trends in employee jobs have been markedly different. Strong self-employment figures have come alongside encouraging employee numbers in some regions like London and the East but have been complemented by steep falls in employee numbers in Scotland and much of the North. There is some evidence that higher unemployment may be linked to growing self-employment.
- Though only a minority (27 per cent) of those who became self-employed in the post-recession years did so due to a lack of better work alternatives, this figure represents a big increase on the proportion of those who became self-employed more than five years ago who did so due to a lack of other work options (10 per cent).

These signs point towards some slack remaining hidden beneath the strong self-employment figures. While it is difficult to quantify the extent to which spare capacity remains, how this picture develops over coming months and years will be an important consideration in debates over when interest rates should start to rise.

Alongside what this means for the economy, we have looked at how self-employed people are faring financially. Our analysis finds that self-employed weekly earnings are 20 per cent lower than they were in 2006-07, while employee earnings have fallen by just 6 per cent. The drop has been seen across genders and industries but is particularly notable among people of prime earning age (35 to 50 years old) whose earnings are 26 per cent lower. As a result, the typical self-employed person now earns 40 per cent less than the typical employed person. Part of the pay drop for the self-employed is down to a reduction in the hours they

are now working and part is likely to be due to a shift in the composition of the group, such as a rise in the proportion of the self-employed who are women.

The analysis paints a **worrying picture of the security and vulnerability of self-employed people** on both a short and long term horizon. Only 30 per cent of self-employed people have any kind of pension, compared with 52 per cent of employees. Our survey also indicates that a minority of self-employed people are experiencing difficulties getting mortgages, tenancies and accessing personal credit and loans, specifically due to being self-employed.

The self-employed now account for one in every seven people in employment. While there are some signs that weak employee vacancies in recent years have contributed to this, on balance it seems likely that relatively high levels of self-employment are here to stay. Despite that, the strength of the headline self-employment numbers seems to have relied heavily on the flexibility of the self-employed, who have faced underemployment and falling earnings. Monitoring how the hours and earnings of this growing part of the workforce recover in coming years will be crucial for understanding the nature of the recovery beyond the overall jobs and wage figures. This is challenging because despite comprising a large section of the workforce, most official metrics do not take account of their earnings.

Moreover, if high levels of self-employment are set to be a permanent feature, it is crucial that this 15 per cent of the workforce are able to access basics such as housing and credit and have sufficient pensions and savings. Our analysis suggests that for too many self-employed people, these essentials are proving difficult to access with many looking to be poorly positioned to cope with unexpected financial demands and retirement. Reform of the mortgage market, the pensions system and the introduction of Universal Credit should take into account the needs of this ever-larger group.

Introduction

The self-employment debate

Since the recovery began, the growth of self-employment has been much stronger than that of employees. While the number of employees has only recently regained its pre-recession level, currently standing at 25.6 million, the number of people who are self-employed has grown by 650,000 since 2008. At the onset of the recession, just under 3.8 million people were self-employed in the UK, equivalent to 13.1 per cent of total employment. By February 2014, that had risen to 4.5 million people or one in every seven workers (14.8 per cent). Despite seeing its fastest growth since the downturn, the uptick in self-employment pre-dates 2008; since the turn of the millennium, an extra 1.25 million people have become self-employed.¹

Much has been written about what exactly this trend represents, with self-employment acting as a bell weather for the underlying strength and direction of the economy. For some, it is an indication that the recovery is built on shaky ground: there are suspicions that many of the newly self-employed are there unwillingly, forced to go it alone due either to the lack of employee jobs or unscrupulous employers looking to minimise their liabilities. There are also claims that people who may previously have remained unemployed have been encouraged to register as self-employed to access tax credits but without the skills or desire to make an enterprise successful. Seen through this lens, self-employment represents another kind of precarious work, in the same vein as zero-hours contracts.

For others, the uptick in self-employment is held up as one of the success stories of recent years. While in previous recessions, those who lost their jobs moved into unemployment or inactivity, this time around a growing entrepreneurial spark is claimed to have resulted in many more setting up their own business. Government support, through schemes like the New Enterprise Allowance, is seen as having contributed to the growth in self-employment with emphasis placed upon the contribution that higher-skilled self-employment has made. Proponents of this view often interpret the rise as people choosing to escape the comparatively heavy burden of tax faced by employees, and preferring the freedom and flexibility which working for yourself can offer, noting that the number of people who are self-employed began to rise in the early-2000s, prior to the recession.

For those who choose it, self-employment can be a challenging but highly rewarding endeavour. But self-employment also brings with it disadvantages, additional struggles and unpredictability. In addition, a range of protections — from basic employment rights to financial security, such as inclusion in auto-enrolment pension schemes — which most employees will enjoy are not available to those working for themselves. As a result, it is important that self-employment should be a genuine choice, not a last resort.

While this debate is important for the individuals involved, in terms of the choice and difficulties they face, there are larger questions to which the rise in self-employment may

¹ Differentiating between (a) increases in the share of total employment accounted for by self-employed and (b) increases in the raw numbers of the self-employed is important given that the UK's population and workforce continue to grow. Although headline figures on the ever-higher number of self-employed people appear particularly notable, the rate may in fact tell us more about how the balance of the UK's labour market is shifting.

suggest answers. Chief among these is the issue of exactly how much slack remains in the economy. Although the centrality of the unemployment rate in determining when interest rates may rise has lessened since the Bank of England introduced additional factors to its forward guidance, the issue of how much spare capacity the growth in self-employment is concealing is an important consideration for the Monetary Policy Committee (MPC). If a section of the self-employed are doing a few hours of “odd jobs” just to get by, with a preference to be an employee, job creation will need to go over and beyond the level that the current unemployment rate of 6.9 per cent suggests. The minutes of April’s meeting of the MPC confirmed the relevance of self-employment but also underlined the diversity of views held on exactly how much slack self-employment is concealing.

What will this report do?

Various, and often conflicting, points of evidence have been used to make the case for both sides of the argument. It is clear that the increasing number of people becoming self-employed is a vital issue that needs to be better understood. Through an analysis of national data sets and a survey, this report presents an investigation into the rise of self-employment. It attempts to answer a number of questions posed by recent trends in the labour market centred around self-employment:

- How has self-employment grown recently and what explains the growth in self-employment?
- How has the overall profile of the self-employed changed since the recession, in terms of their characteristics and working patterns?
- How does the financial security of the self-employed compare with that of employees?

This note does not attempt to answer every question related to the rise of self-employment, such as its role in explaining the UK’s productivity puzzle or its influence on business investment. Nor does it offer policy prescriptions. This will be the subject of future work by the Resolution Foundation.

In order to answer these questions, this note will draw primarily upon analysis of the Labour Force Survey (LFS) and Family Resources Survey (FRS), cross-checked with the Bank of England NMG survey where appropriate. Data from EUROSTAT and the OECD are used to position the UK internationally. When analysis moves beyond the headline numbers, the data used covers a time period up to the end of 2013 at the very latest, and frequently earlier than this. This means that much of the analysis will not capture the very recent strong uptick in self-employment, and may therefore understate certain trends.

This note also discusses a survey of 985 self-employed people, conducted by Ipsos MORI and commissioned by the Resolution Foundation for this report. Fieldwork took place between 28 March and 7 April 2014 and was carried out online. The figures have been weighted and are representative of all self-employed adults in Great Britain aged 16-65. All percentages from the Ipsos MORI survey exclude those who responded ‘don’t know’, ‘can’t remember’, ‘not applicable’, or who refused to answer the question, from the base.

Defining self-employment

As with many commonly used employment categories, self-employment does not have a single, legal definition. A variety of definitions are potentially relevant and are used in different contexts, with further gradations below the headline definition. Occasionally these definitions can be contradictory e.g. a person may be considered self-employed for tax purposes but may be treated differently when considering employment rights. According to HMRC, you are probably self-employed if you:

- run your own business and take responsibility for its success or failure
- have several customers at the same time
- can decide how, when and where you do your work
- are free to hire other people to do the work for you or help you at your own expense
- provide the main items of equipment to do your work

As will be discussed below, the Labour Force Survey (LFS) uses a number of sub-categories below its headline question “Were you working as an employee or were you self-employed?” (also used in OECD data), which relate to the ways in which self-employed people are paid for the work that they do. While some inferences can be drawn from these terms, their usefulness is limited because the respondent is left to decide which category fits them best, they can choose more than one category and no full description is provided. Because of that, the categories below from the LFS should be treated with caution as they do not relate to any legal definition:

- a sole director of your own limited business
- running a business or professional practice
- a partner in a business or professional practice
- working for yourself
- a sub-contractor
- doing freelance work

These categories are sometimes linked to broad typologies of the self-employed, separating out those in charge of a business or professional practice or highly-skilled freelancers, from tradespeople who work for themselves or as a sub-contractor. These are very loose types and will conceal a variety of different experiences and skill sets.

The definition used in this note other than when specified refers to people for whom self-employment is their only source of income as well as those who are primarily self-employed and are an employee as a second job. It does not include those who are primarily an employee but self-employed in a second job.

When European data are referred to, the following definition from EUROSTAT is taken to apply to participating countries:

Self-employed persons are the ones who work in their own business, farm or professional practice. A self-employed person is considered to be working if she/he meets one of the following criteria: works for the purpose of earning profit, spends time on the operation of a business or is in the process of setting up his/her business.

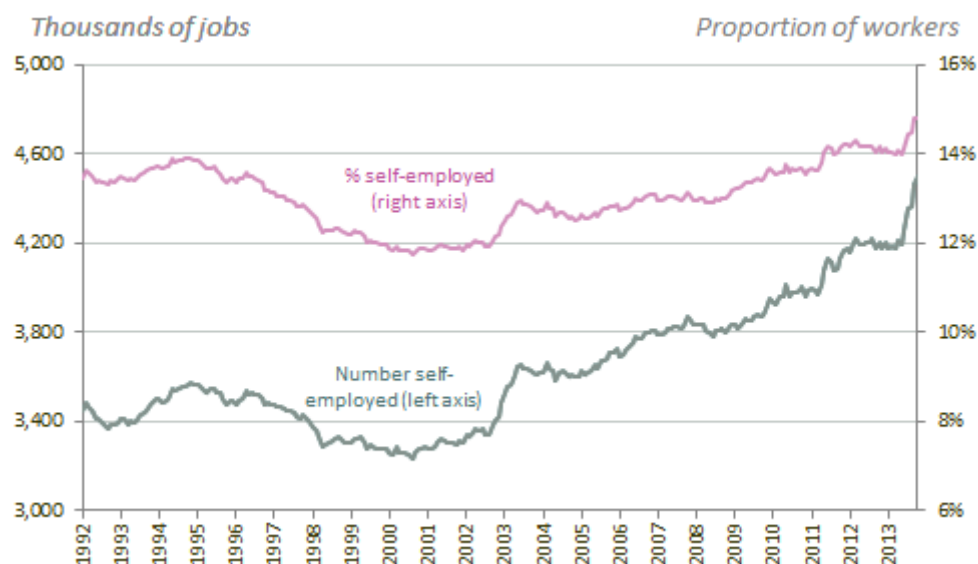
An overview of self-employment in the UK

This chapter looks in detail at how self-employment levels in the UK, and the characteristics and working patterns of the self-employed, have changed in recent decades and particularly since the recession. It also contextualises these changes from an international perspective.

Self-employment over time

Rising self-employment since the recession has received much recent attention, but the upward trajectory of the self-employed as a proportion of UK workers dates back to the 1960s. In 1966, just 6.7 per cent of UK workers were self-employed. This figure rose throughout the 1970s and 1980s to reach 13.8 per cent of workers in 1996.² Self-employment then fell slightly through the late 1990s and early 2000s,³ and it is only since the financial crash that the proportion of workers who are self-employed has risen back above the 1990s peak, as shown in Figure 1.

Figure 1: Self-employment since 1992⁴



Source: Labour Force Survey, ONS.

Since the beginning of the recession, the number of self-employed people has risen by over 650,000, while employee jobs have only recently returned to pre-crisis levels, as illustrated in Figure 2. As a result, in the latest data, self-employment accounts for the majority (81 per cent) of the net change in total employment since early 2008. However, the contribution of self-employment to overall employment changes depending on the starting point picked (for example, measuring since 2007, Morgan Stanley research recently cited a figure of 83 per

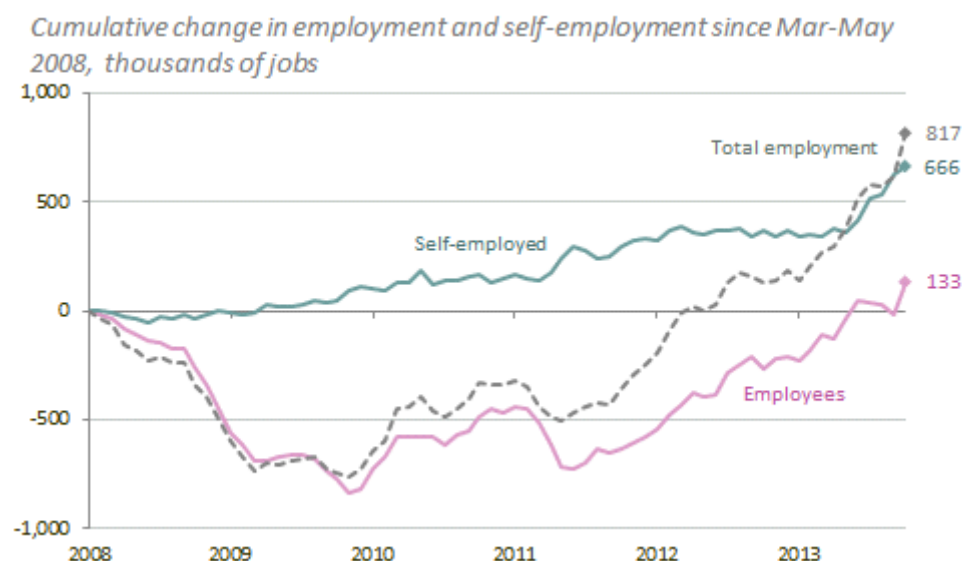
² Blanchflower, D.G., (2000). "Self-employment in OECD countries," *Labour Economics*, vol. 7(5), p. 471-505, September.

³ The rise during 2001 and 2003 was explored by the Office for National Statistics at the time and found to be not unprecedented and consistent with the economic climate. There were no changes in survey design or the tax system that were identified as contributing to this rise. See: Lindsay, C. and Macaulay, C. (2004) "Growth in self-employment in the UK", Office for National Statistics, *Labour Market Trends*, October 2004.

⁴ Unless otherwise stated, all figures and analysis in this report refer to the UK.

cent, and measuring since the election the Trades Union Congress cited 44 per cent), and masks significant variation in both employee and self-employed jobs over the period.^{5 6}

Figure 2: Change in employment and self-employment since the pre-recession employment peak



Notes: Total employment also includes unpaid family workers and those on government employment and training schemes.
Source: Labour Force Survey, ONS.

The share of the UK workforce that is self-employed looks unremarkable when compared internationally in the latest data, with the rate of self-employment in the UK ranking slightly below average in comparison to other countries in the OECD, as Figure 3 shows. But focusing on averages conceals the variety of experiences across countries. While the US, Norway and Luxembourg all have self-employment rates of 7 per cent or lower, in Turkey, Greece and Mexico, one in every three workers is self-employed. Considering a different group of countries, the G7 (highlighted in dark pink), only Italy has a higher rate of self-employment than the UK.

While the UK's self-employment level currently lies close to the international average, where it does differ is in the trend over the past few decades. The 1966-1996 increase in the proportion of self-employed workers in the UK was in contrast to the experience of most other OECD countries, where self-employment became a smaller part of total employment.⁷ This trend plateaued at the turn of the century before starting to rise again. The UK was one of only a handful of developed economies in which self-employment as a share of total employment rose from 2000 to 2011, growing by 8 per cent across the period, while the OECD and EU27 averages both fell by 9 per cent.

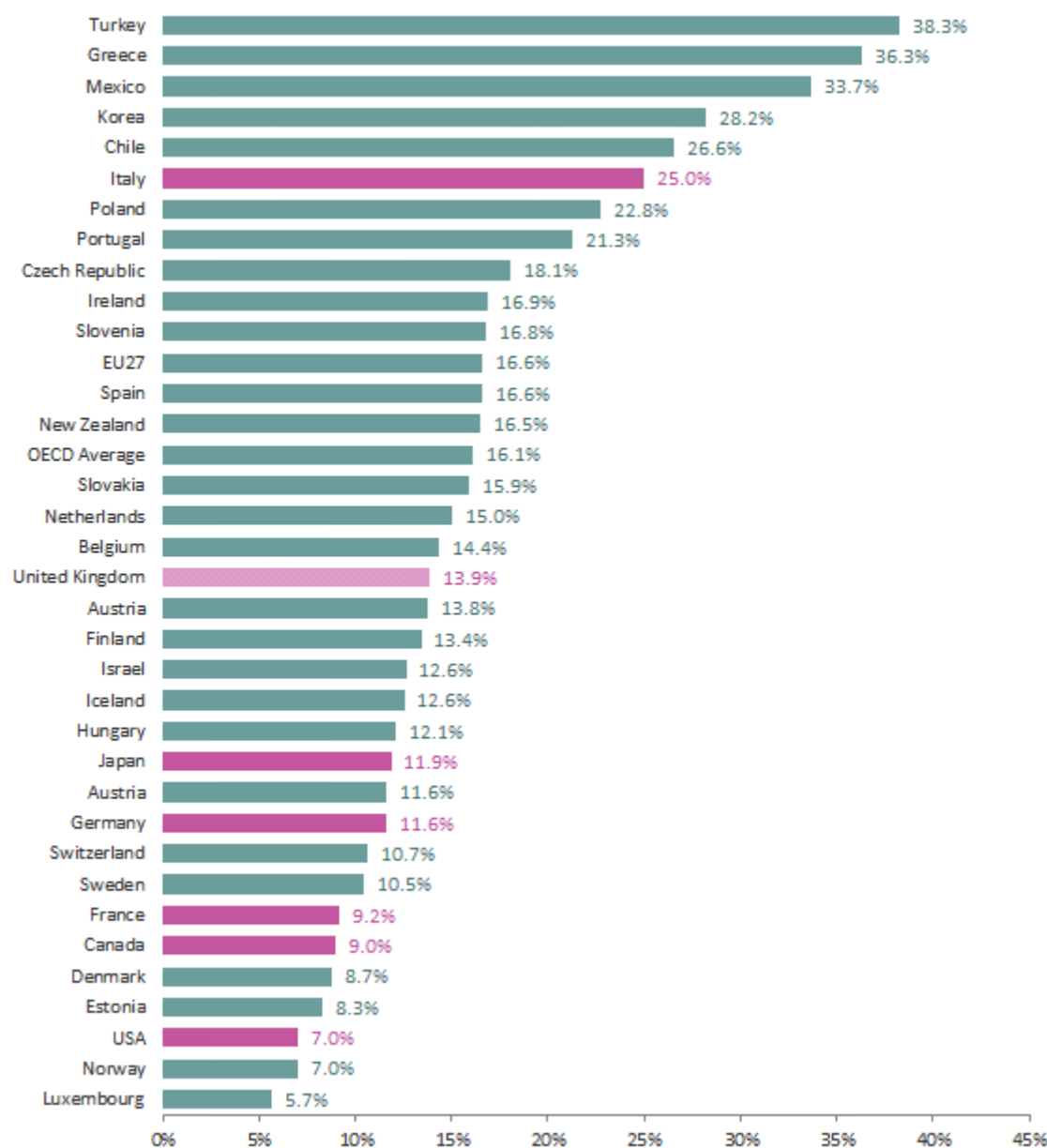
⁵ Ashworth, J. et al, (2014) "The UK's self-employment phenomenon: why the labour market isn't so strong after all", Morgan Stanley Research

⁶ www.tuc.org.uk/economic-issues/economic-analysis/labour-market/labour-market-and-economic-reports/more-two-five-new

⁷ Blanchflower, D.G., (2000)

Figure 3: Self-employment rates in OECD countries

Self-employment as a share of total employment, 2011 or latest available data



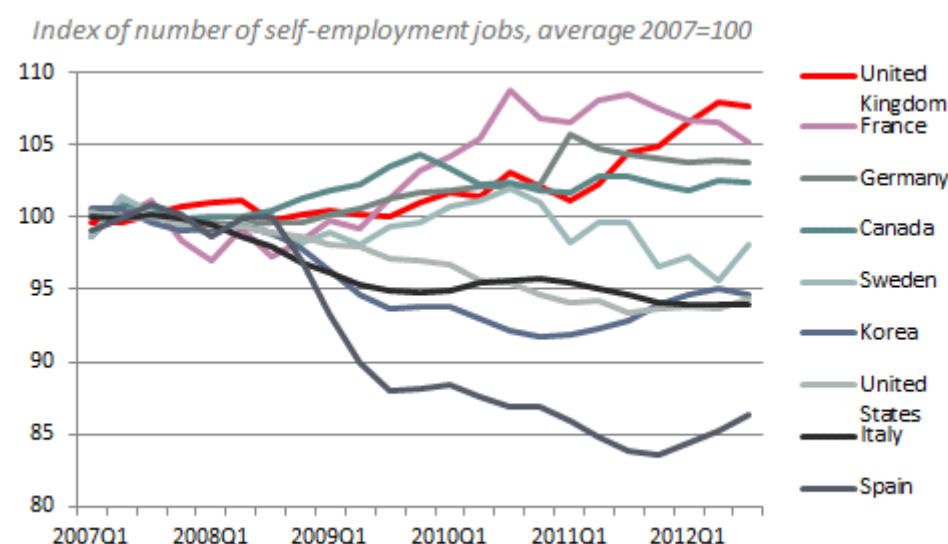
Notes: The UK figure on this chart is not as up-to-date as those reported elsewhere in this report in order to be consistent with international data.

Source: Resolution Foundation analysis of stats. OECD.

Focusing on the period since the financial crash tells a similar story. As Figure 4 highlights, the UK saw a larger relative increase in the number of people self-employed between 2007 and the third quarter of 2013 than many other advanced economies.⁸ Whether considering the short- or long-term increase in self-employment, the change in the UK workforce has consistently bucked international trends, meaning that we are looking at a phenomenon that is particular to the UK labour market.

⁸ Some of which is likely to be driven by differences in population growth and changes in total employment.

Figure 4: Change in self-employment rates in selected OECD countries since 2007



Source: *Entrepreneurship at a glance 2013*, OECD

Internationally, what accounts for higher or lower self-employment?

What explains this variation? A cross-OECD analysis of what drives self-employment growth highlighted the importance of the relative attractiveness of taxation of the self-employed and the replacement rates offered by unemployment, as well as the female labour force participation rate.⁹ The weight of evidence on the relationship between self-employment and unemployment appears to indicate a positive relationship between unemployment and self-employment rates (that is, higher levels of self-employment tend to occur alongside higher levels of unemployment, although conflicting factors are at work.¹⁰ Again, this will depend on interaction with the tax and benefit system, in terms of how much support is available to the self-employed, in the form of tax credits or other benefits. Later sections of this report will examine the evidence for a link in the UK in more detail.¹¹ However, no easy conclusions can be drawn from international comparison. Economies as diverse as the US, Norway and Luxembourg have some of the lowest rates of self-employment while South Korea, Italy and Portugal all have high levels.

Characteristics of the self-employed

The characteristics of self-employed people are different to employees in some respects and similar in others—in particular they are much less likely to be female and much more likely to be aged over 50, as shown in Figure 5. Figure 5 also reveals that the change in the composition of the self-employed since 2005 (which is when the overall employment rate

⁹ Parker, S. C. and Robson, M. T. (2004) 'Explaining international variations in self-employment : evidence from a panel of OECD countries.', *Southern economic journal*, 71 (2). pp. 287-301.

¹⁰ See for example Carmona, M et al., (2013) "Does Unemployment Respond Asymmetrically to Self-Employment Shocks? Evidence from a Panel of 23 OECD Countries", Thurik, A. et al., (2007) "Does self-employment reduce unemployment?", *Jena economic research papers*, No.2007,089 and Blanchflower, D.G., (2000)

¹¹ The World Bank's *Doing Business* series looks at a range of factors affecting the self-employed. On the issue of ease of Starting a Business, the UK's ranking fell from 2013 to 2014, from 18th to 28th place internationally, suggesting that there has been no major alleviation of the difficulty of setting up a business which would make self-employment a more attractive prospect.

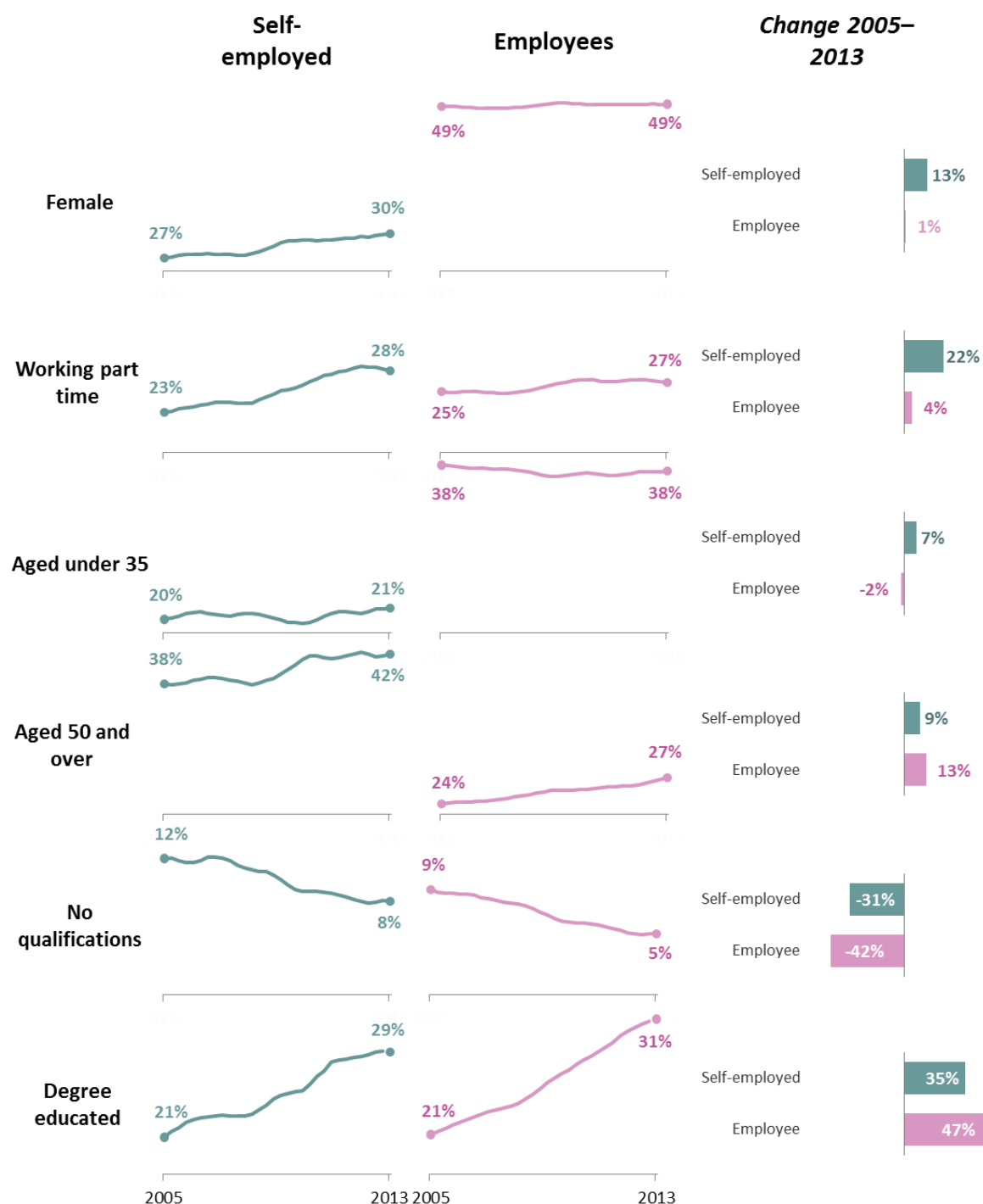
peaked during the boom years) has been similar to that among employees: both have been getting older and more qualified, and both are now more likely to work part-time (although the rise among the self-employed has been steeper).

Trends related to the age of the self-employed merit particular attention, as older workers have been credited with driving the recent growth in self-employment.¹² Although discussed quite widely, much of the growth in the share of over-50s among the self-employed is matched among employees, and thus appears to be due to an ageing workforce. This measure, shown in Figure 5 below, provides a more complete picture than looking at the changing age profile of the self-employed in isolation. Subsequent sections of this report will discuss trends related to ageing and self-employment in more detail.

The exception to these similar trends among self-employed people and employees is that women now make up a greater proportion of the self-employed than they did in 2005, although they are still less likely to be self-employed than men, whereas the gender composition of employees has stayed the same.

¹² See for example: <http://www.tuc.org.uk/economic-issues/economic-analysis/labour-market/labour-market-and-economic-reports/more-two-five-new>

Figure 5: Characteristics of the self-employed and employees in the UK and change since 2005



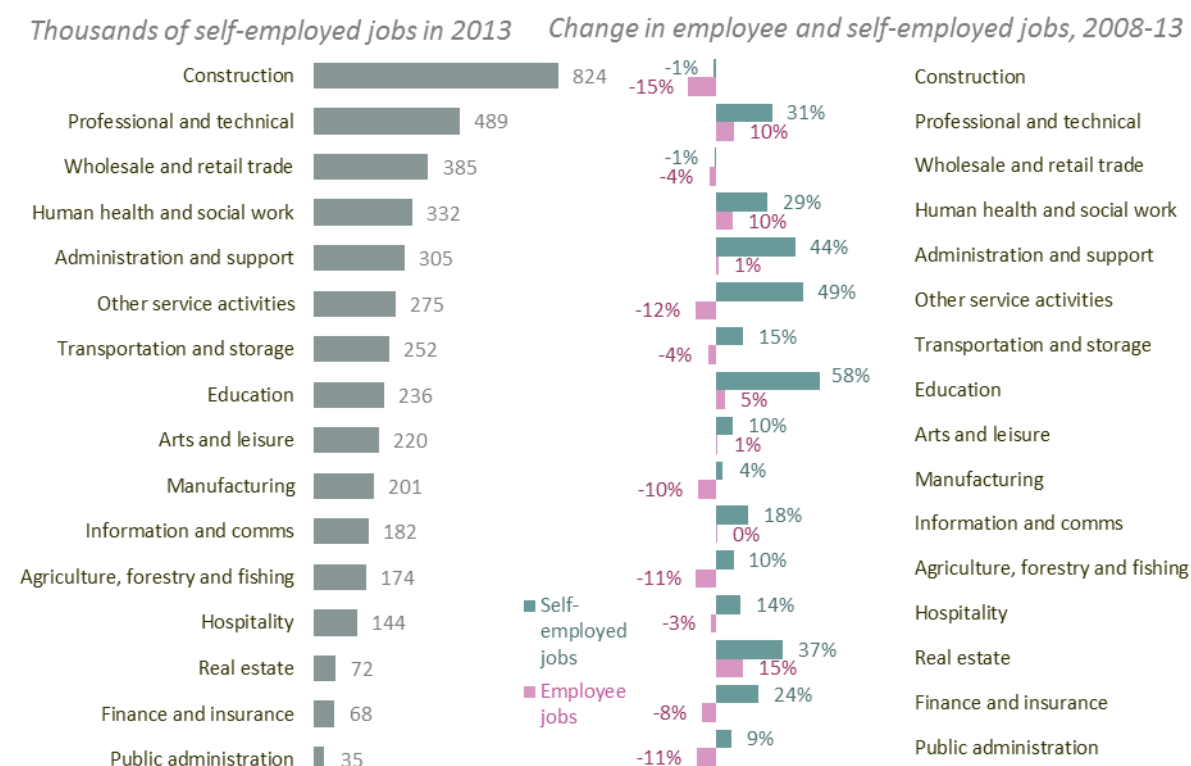
Notes: Charts display four-quarter rolling averages running from April 2005–March 2006 to January–December 2013.

Source: Quarterly Labour Force Survey, ONS.

Self-employment exists across all sectors of the UK economy, with by far the largest number of self-employed people working in the construction sector. However, as Figure 6 shows, it is often more knowledge-intensive service sectors that have seen the biggest proportionate increases in self-employed jobs since around the start of the recession in 2008. For the most part, these are sectors that have also seen increases in employee jobs, reflecting broader structural trends towards an increasingly service-led economy. In some sectors, such as

education and public administration, given the rise in self-employed jobs and the fall or small growth in employee roles, changes to public funding and the need to reduce costs may have played a role.¹³

Figure 6: Self-employed jobs across industries and change since 2008



Notes: Four-quarter rolling average. Industries with fewer than 10,000 self-employed jobs have been excluded. Source: Workforce Jobs, ONS.¹⁴

Comparing the characteristics of the self-employed internationally, it is notable that women make up a smaller proportion of self-employed people relative to men in the UK than in most other OECD countries. The UK is one of only a handful of countries in which the self-employment rate of women is less than half that of men.¹⁵

The qualifications of self-employed people in the UK are more in line with international trends, at least within Europe. As Figure 7 shows, the UK has a slightly higher than average proportion of skilled people working as self-employed, although not as high as the major

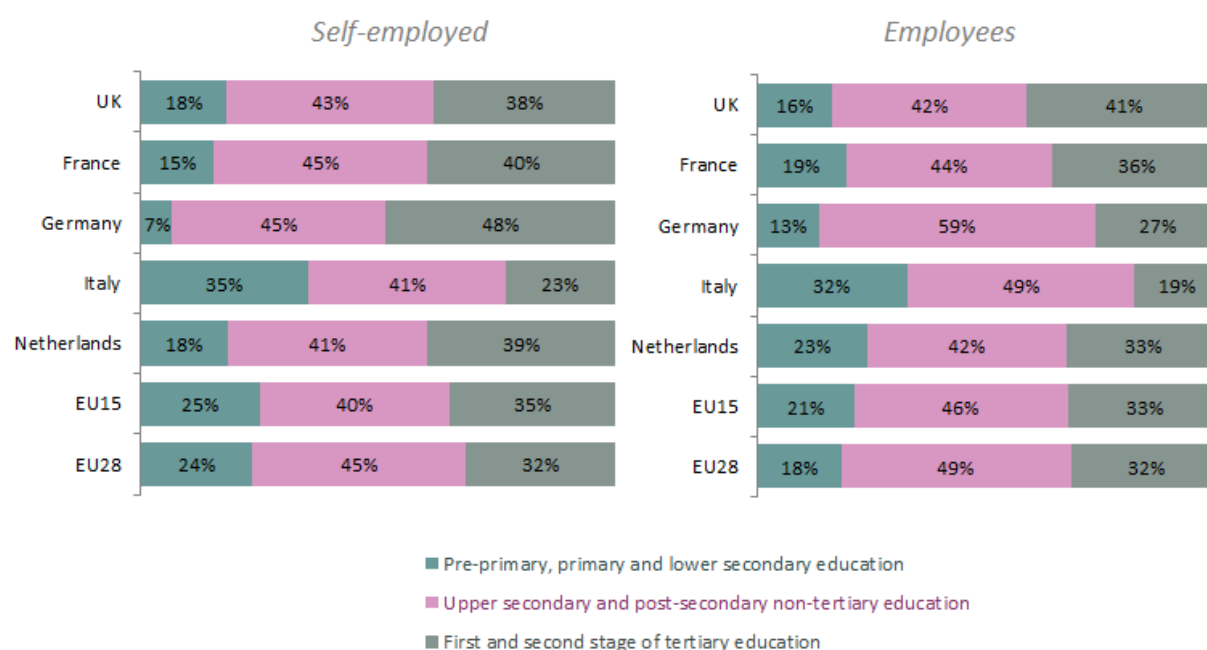
¹³ Evidence presented to the Select Committee on Personal Service Companies (the name given to the legal entities used by self-employed individuals) by the National Association of Schoolmasters Union of Women Teachers (NASUWT) referred to the practice by which the majority of supply teachers find work through recruitment agencies and are likely to be considered self-employed, although the use of umbrella companies complicates their employment status. For further discussion, see: <http://www.parliament.uk/documents/lords-committees/Personal-Service-Companies/personalservicecompaniesvolume.pdf>

¹⁴ The Workforce Jobs dataset has been used as it is the preferred source for measuring change in jobs by industry. This dataset combines a range of employer surveys, household surveys and administrative sources, relying on household surveys to measure self-employed jobs, and employer surveys to measure employee jobs. It is possible that employers and self-employed individuals understand industrial classifications in a different way, which may lead to some inconsistencies between the two. This figure displays industries according to the more up-to-date SIC 2007 classifications, however in subsequent sections of this report SIC 1992 codes are used as consistent SIC 2007 codes are not available across the time-series.

¹⁵ Resolution Foundation analysis of OECD (2013), *Entrepreneurship at a Glance, 2013*.

European economies of Germany and France. The trend from 2007 to 2013 in each of these groups has been relatively uniform across countries, with the percentage of less educated self-employed workers and more educated self-employed workers both rising, likely reflecting structural shifts in the skills composition of the international workforce. Comparison of the occupational level at which self-employed people work across Europe produces a similar picture, with the UK occupational profile in line with other major EU economies and not dissimilar from that of employees.¹⁶

Figure 7: European comparison of the qualifications of the self-employed and employees, 2013



Notes: chart displays four-quarter rolling averages for all self-employed people and employees aged 15-74.

Source: Resolution Foundation analysis of EUROSTAT.

Overall, the profile of self-employed people in the UK, and how this has changed in recent years, is broadly in line with both changes in the profile of UK employees and the characteristics of self-employed people in other countries. The main exception to this is that women are growing as a share of the self-employed—which is not the case for employees—but female self-employment continues to remain far below international levels.

Change in self-employment across regions

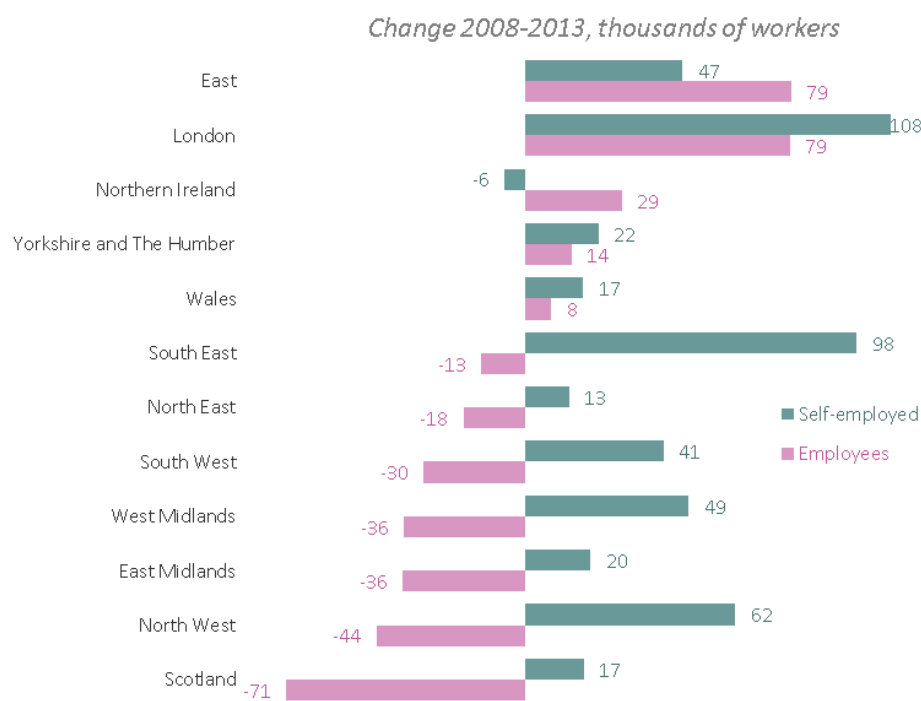
Recent growth in self-employment has been spread across regions of the UK, with increases in all regions apart from Northern Ireland since the onset of recession in 2008. However, as Figure 8 below shows, this pattern has been in marked contrast to changes in employee numbers across regions, more than half of which had not recovered the employees lost during the recession by 2013.¹⁷ In contrast, when comparing the changes in the self-

¹⁶ The difference in Germany is perceived to be a result of their education system and its strong vocational element.

¹⁷ Looking, over the same period, at where jobs are (rather than where workers live), the picture becomes even starker. Only in London had employee jobs outstripped self-employed jobs, and the number of employee jobs had fallen everywhere except London and the East of England. See Annex for a full breakdown. Source: Workforce Jobs, ONS.

employed and employees since the national employment recovery began in early 2010 (i.e. following the recession period when employees lost jobs in large numbers), in nearly half the regions of Great Britain (the West Midlands, the South West, the North West, the North East and Scotland) the self-employed grew more than employees (see Annex for a full breakdown).

Figure 8: Changes in regional self-employment and employees since 2008



Source: Annual Population Survey, ONS.

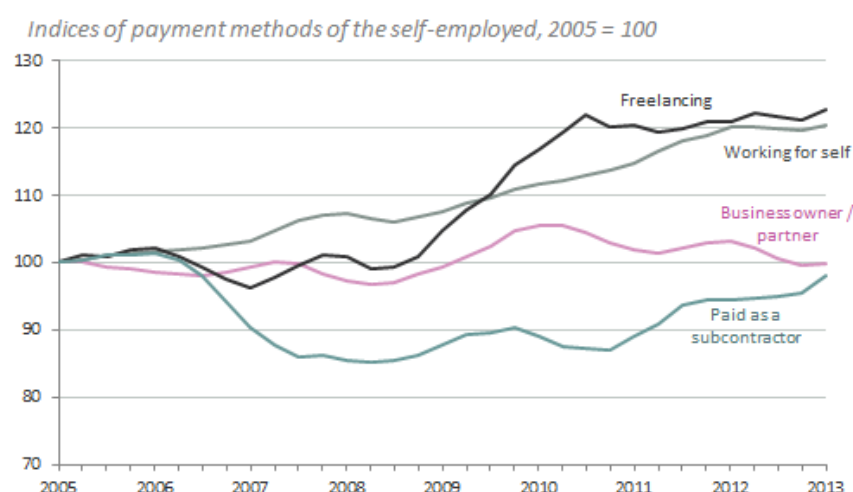
Status and outlook of the self-employed

For those who see high rates of self-employment as positive, much is made of the entrepreneurialism and innovation associated with going it alone. To what extent is that borne out by the data? Those more suspicious of the growth of self-employment worry about it representing people who would prefer the security and protection that comes with an employee role.

What's in a name?

The way in which the self-employed describe the kind of self-employment they are engaged in is far from representing legal or even clearly understood definitions. However, the way in which self-employed people are paid is illuminating of the type of work they are doing. The two categories (they can be in more than one category at the same time) that self-employed people most commonly identify with are 'working for themselves' (71 per cent) and being a business owner or partner (38 per cent). Figure 9 shows that while business ownership has remained flat since 2005, the number of self-employed people who identify as 'working for themselves' has risen steadily. The number identifying as freelancers does seem to have increased following the recession, but still only 14 per cent of the self-employed identify with this payment status. Overall, the ways in which the self-employed are paid seem to suggest a rise in freelancing that looks partly cyclical (although there are still only a small minority of freelancers), with long-term trends being otherwise maintained.

Figure 9: Change in payment methods of the self-employed



Notes: Four-quarter rolling average. Self-employed people can be in more than one category at the same time. The numbers 'paid a salary or wage by an agency' are not displayed due to low sample numbers.

Source: Quarterly Labour Force Survey, ONS.

'Doubling up'

Underneath the headline rise in self-employment, the past eight years have seen growth in people 'doubling up': combining self-employment with being an employee. The headline numbers count everyone who is self-employed as their main job, which includes a minority of people who also have a job as an employee. Although, only 90,000 (2 per cent) of those who are self-employed people are in this category, Figure 10 shows that their numbers swelled prior to the recession and have stayed elevated since. Figure 10 also shows an increase prior to and during the recession in the number of people whose main employment status is an employee, but who are self-employed in their second job. There are now 320,000 people in this position, or 1 per cent of all employees. These people are not counted in the headline self-employment statistics as they are not considered to be primarily self-employed; if they were, they would inflate the figure by 7 per cent.

Figure 10: Change in levels of self-employment status



Notes: Four-quarter rolling average.

Source: Two-Quarter Longitudinal Labour Force Survey, ONS

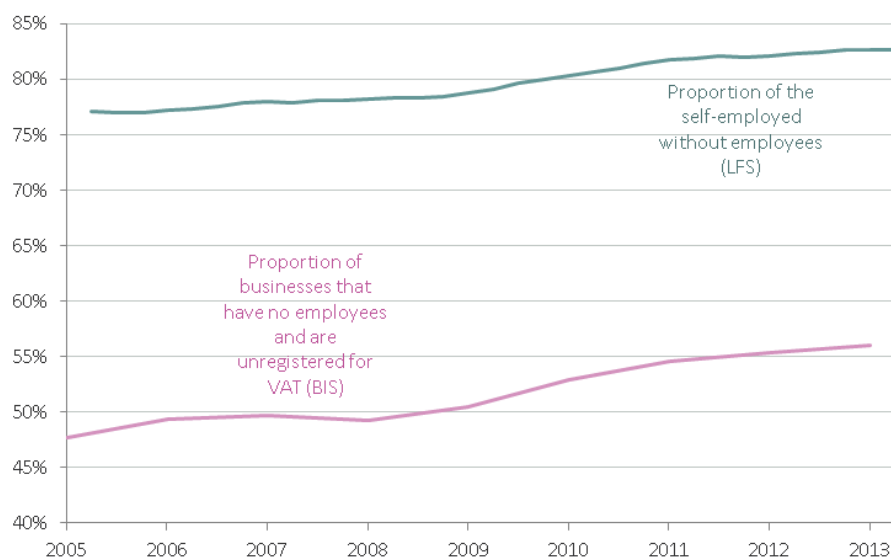
Although they remain a small minority, the strong increase in the numbers ‘doubling up’ suggests a growing propensity to combine self-employment with other types of working. And while ‘doubling up’ could be construed mainly as a response to a tough economic climate, the increase seems to largely pre-date the financial crash.

Start-ups or one man bands?

The growth in self-employment is often depicted as representing a spike in entrepreneurialism. Our survey conducted by Ipsos MORI of just under 1,000 self-employed people suggests that “entrepreneur” is not a label most would assign themselves. Excluding those who said they didn’t know, only a third (34 per cent) of respondents consider themselves to be an entrepreneur. With any survey question, it is difficult to ascertain exactly what is being considered by the respondent but it suggests that the majority of the self-employed are not engaged in innovative or risky ventures.

There appears to be a gentle and steady trend towards self-employed people genuinely going it alone, likely to be connected to the growth in the number of self-employed people either paid as a freelancer or by working for themselves, as shown above. Figure 11 shows that the proportion of self-employed people who do not employ anyone else has risen from 77 per cent in 2005 to 83 per cent in 2013. There appears to have been a slight acceleration in the trend at the end of the recession, but it is not particularly marked. As a comparator, business estimates similarly show that a growing proportion do not employ anyone and are also too small to register for VAT. Again there appears to be a slight recessionary acceleration within a longer-term upward trend.

Figure 11: self-employed people and businesses without employees



Notes: Four-quarter rolling average used in the Labour Force Survey. The two lines on this chart have different bases, as not all self-employed people are business owners, and not all business are run by someone who would describe themselves as self-employed.

Source: Quarterly Labour Force Survey, ONS and Annual Business Population Estimates, BIS.

Interestingly, the proportion of self-employed people without employees in the UK stands out as the highest of the major European economies. For example, while 83 per cent of self-employed do not employ anyone else in the UK, the equivalent figure for France is 60 per

cent, and just 56 per cent in Germany.¹⁸ Overall, then, the proportion of self-employed people going it alone appears to be on a sustained upward trajectory, and marks the UK out in comparison to other European countries.

Summary

This chapter has highlighted that the strong growth in self-employment since the recession builds on decades of increasing self-employment in the UK, in stark contrast to trends in most other countries. The very high share of net jobs growth since the recession accounted for by self-employment masks what has been going on during the recession and recovery: self-employment has risen steadily (at least until recently when growth accelerated), while employee jobs fell sharply and have just climbed out of the trough. In addition, we have seen that changing characteristics of the self-employed are mainly mirrored among employees and that the UK's self-employed have relatively similar characteristics to self-employed people elsewhere, indicating that some trends in self-employment may be strongly connected to broader and more structural labour market patterns. Although self-employment growth has been relatively broad-based across regions, trends in employee jobs have been markedly different, suggesting regional imbalances in the role self-employment is playing in the labour market.

These findings help us to understand what is driving the growth in self-employment and what this growth means for the economy and the recovery, but they only tell some of the story. The overall change in self-employment is a balance of changes in people who are actually becoming self-employed and changes in people leaving self-employment. And within this it is essential to understand where those people who have made the leap into self-employment are coming from and what motivated them to do so. The following chapter will address these questions.

¹⁸ Source: Eurostat, 2013 figures.

What explains the growth?

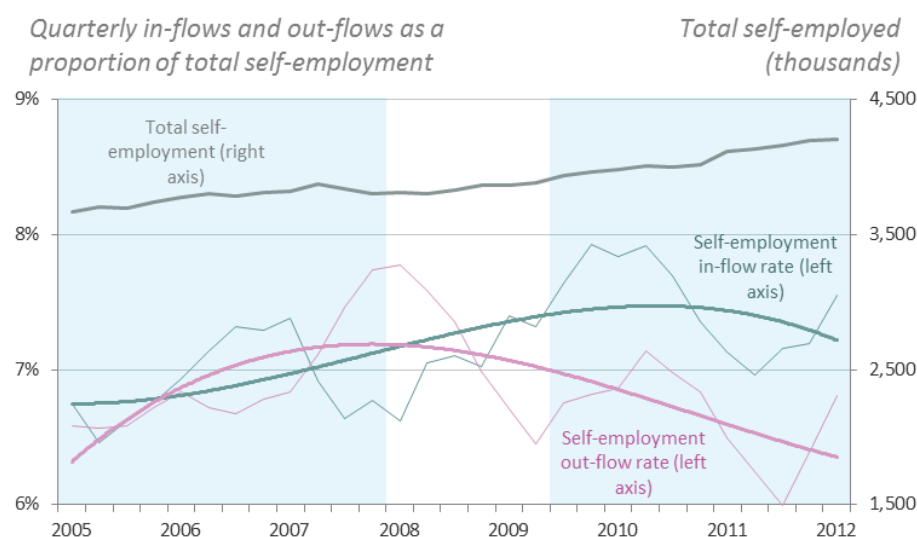
This chapter looks beneath the headline self-employment numbers to further understand the drivers of self-employment growth, focusing on the period since the end of the recession in late 2009. Specifically, we disaggregate the opposing effects of new people becoming self-employed and people leaving self-employment. In terms of those becoming self-employed, we explore the characteristics of people moving into self-employment since the recession in comparison to the pre-recession years in order to understand whether there has been any change in the new starters. And we look at the role of unemployment, and unemployment-focused labour market policy in the form of the New Enterprise Allowance and welfare reforms, in stimulating self-employment growth. In terms of people leaving self-employment, we explore what might be driving the self-employed to remain self-employed for longer.

New starters of just fewer leavers?

The total number of self-employed is a result of both the gross number of people that become self-employed in a given month, quarter or year, and the number of people who leave self-employment over the same period. Increasing self-employment will be due to an increase in the 'in-flow' rate (i.e. the number of new starters as a proportion of the total self-employed), or a decrease in the 'out-flow' rate (i.e. the number of leavers as a proportion of the total), or (more likely) a combination of both.

This is exactly what we have seen in recent years. Although the trends are quite volatile, Figure 12 shows that the self-employment in-flow and out-flow rates were very close to one another in the period prior to the pre-recession employment peak (shown by the first shaded blue box), but in the years since total employment hit its post-recession low (the second shaded blue box), the in-flow rate has increased on its previous level, while the out-flow rate has decreased.

Figure 12: Self-employment in-flows and out-flows before and after the crisis



Notes: Four-quarter rolling average, with horizontal axis showing mid-points of averages. In-flows and out-flows entail a status change between two consecutive quarters to or from another type of employment (mainly employee jobs), unemployment or inactivity.¹⁹

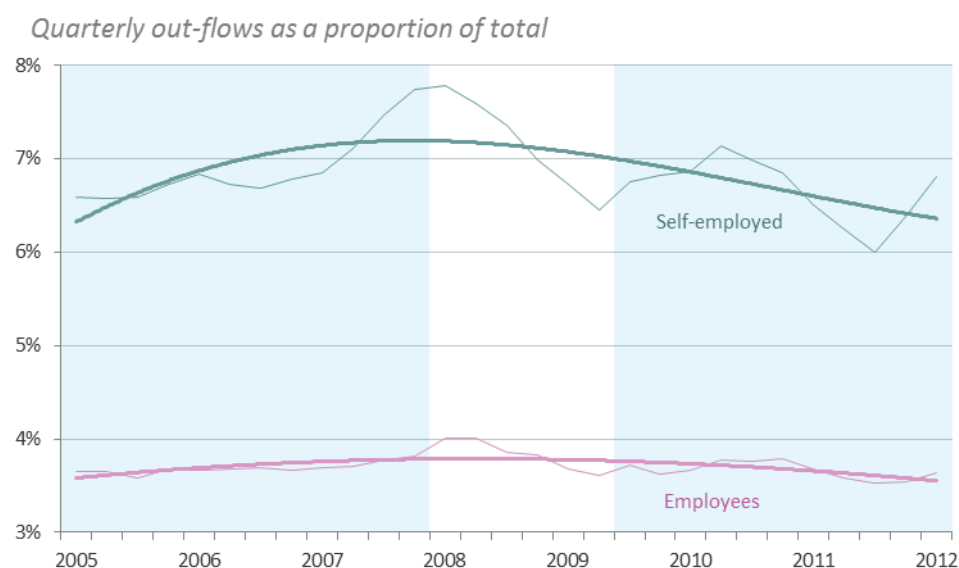
¹⁹ Three-order polynomial trend lines are displayed to estimate the direction of the trend before the crisis, during the crisis and after the crisis. The first shaded period runs up to the peak in total employment at the

Source: Two-Quarter Longitudinal Labour Force Survey, ONS.

To estimate the relative contribution of a rising in-flow rate and a falling out-flow rate to the overall growth in self-employment since the crisis, we can compare the changes in rate between these pre- and post-recession periods. Building on methods for estimating the relative contribution of in-flows and out-flows to changes in unemployment, **we estimate that decline in the rate at which people leave self-employment accounts for over a quarter (28 per cent) of overall self-employment growth over the post-recession period, with a rise in people becoming self-employed accounting for the remaining nearly three quarters (72 per cent).**²⁰

This declining out-flow rate is not seen to the same extent for employees, for whom out-flows have remained relatively flat over the pre- and post-crisis periods, with only a very small decline in recent years as Figure 13 shows.²¹ In other words, the recent increase in employee numbers is much more strongly composed of in-flows (as might be expected following a recession) than the increase in the self-employed.

Figure 13: Self-employed and employee out-flows before and after the crisis



Notes: Notes: Four-quarter rolling average, with horizontal axis showing mid-points of averages.

Source: Two-Quarter Longitudinal Labour Force Survey, ONS.

Who are the new self-employed?

Although a declining out-flow rate looks to have played more of a role in recent self-employment growth than it has for employee growth, the self-employment in-flow rate still plays the dominant part. What do we know about these new starters that account for nearly three-quarters of the overall growth in self-employment?

start of the recession, while the second shaded section covers the period since the total employment 'trough' following the recession.

²⁰ This method creates a ratio of the percentage change in the outflow rate between the pre-recession and post-recession periods and the percentage change in the inflow rate between the two periods. See Smith, J. C. (2011) "The Ins and Outs of UK Unemployment", University of Warwick.

²¹ As an aside, Figure X also highlights that out-flows from self-employment are consistently higher than out-flows from being an employee (as are in-flows), demonstrating the fact that people move into and out of self-employment at a much higher rate than people stop and start being employees. This tells us that self-employment is, and has always been, an employment option with much higher 'churn'. This is perhaps unsurprising, given the relative risks of starting out on your own.

Figure 14 below shows how the characteristics of people who move into self-employment, alongside the characteristics of new employees, compared prior to the total employment peak at the start of the recession, and since the recovery began at the start of 2010. We saw in the previous chapter that self-employed people are generally older than employees, and less likely to be female, and the same is true for those entering self-employment compared to those entering employment. Although the characteristics are quite similar, we can see that those starting out as self-employed since the recession are somewhat older and more qualified than those who became self-employed in the pre-recession period, but exactly the same shift has taken place for employees. However, some divergence does seem to have taken place around gender: **those entering self-employment are now more likely to be female**, which is not the case for employees. In addition, **the share of those entering self-employment who start out working part-time has increased much more than it has for employees**.

Figure 14: characteristics of in-flows to self-employment and being an employee



Source: Two-Quarter Longitudinal Labour Force Survey, ONS.

We also looked at the industries and occupations that those entering self-employment join. The industry profile has not changed very much when comparing the period after the recession to the period before, and those industries where self-employment in-flows have increased have generally also experienced increases in employee in-flows (see Annex for full breakdown by industry). There are some differences, however, for example public administration has been a declining sector among new employees but a growing one among the new self-employed, which may reflect the constraints associated with changes to public funding in recent years.

Looking at occupation, things are broadly unchanged from the pre-recession period. The only shifts are that there are somewhat more people starting out as self-employed in professional occupations (18 per cent of all in-flows in the post-recession period compared to 15 per cent of in-flows pre-recession), and somewhat fewer people starting out as self-employed in skilled trades occupations (17 per cent post-recession compared to 21 per cent pre-recession). These same shifts have taken place in employee in-flows pre- and post-recession (see Annex for full breakdown by occupation).

And where have the new self-employed come from?

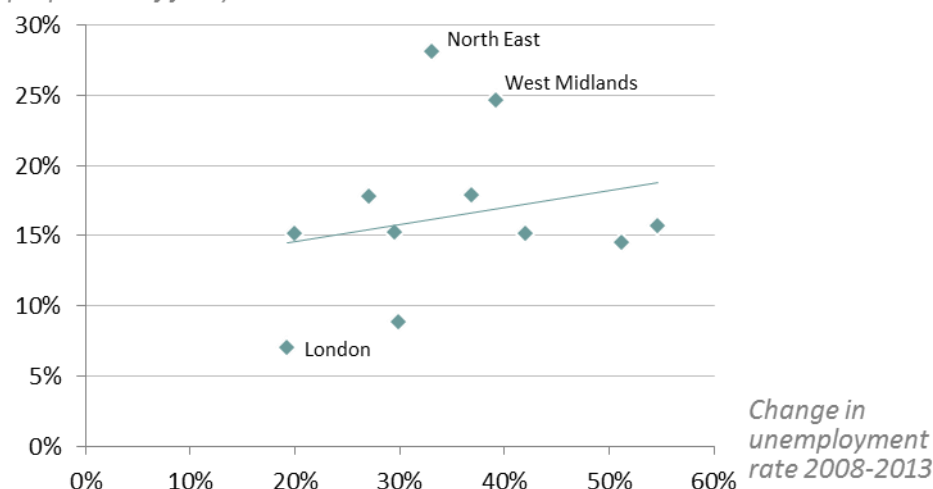
If they don't look particularly different, then can we discern anything from where the new self-employed have come from? We know that employee vacancy levels remained weak even as the employment recovery took shape following the recession, suggesting that self-employment has played a role in driving down (or at least keeping a lid on) unemployment. How much of overall self-employment growth is down to people leaving unemployment who would ordinarily have become employees?

To answer this question we can consider changes in where people who leave unemployment go to, comparing the pre-crisis period to the recovery phase. In the pre-recession period 8 per cent of all those moving from unemployment into work on a quarterly basis became self-employed, while in the recovery period since the beginning of 2010 the figure was 11 per cent. As a straw man, **if this shift had not taken place and the distribution of moves into work from unemployment had remained the same in the post-recession period as it was pre-recession, we estimate that the number of people entering self-employment since the recession would have been up to one-third lower.** Remembering that a greater number of people entering self-employment account for nearly three quarters (72 per cent) of overall self-employment growth since the recession, this suggests that **the shift in the destinations of the unemployed may explain up to a quarter (24 per cent) of the overall growth in self-employment.**

Some support for this link between self-employment growth and unemployment is found at the regional level. We saw in the previous chapter that strong self-employment growth since 2005 has often been coupled with weak employee growth within regions, hinting at a relationship between self-employment and wider local labour market conditions. Further analysis, shown on Figure x, indicates that strong self-employment growth in the West Midlands since the recession, for example, has been coupled with above average unemployment growth, while London has experienced both the lowest (proportionate) self-employment growth and the lowest growth in the unemployment rate. The trend on Figure 15 is too weak to conclude any clear relationship between unemployment and self-employment, and the international evidence for such a relationship, discussed in the previous chapter, is mixed. However, we can certainly conclude that self-employment growth is *not* correlated with strengthening labour markets at the regional level, and observe that self-employment has frequently held up or grown in places where employee jobs have fallen and unemployment has risen.

Figure 15: self-employment growth compared to unemployment growth across regions

Change in self-employment rate (self-employed jobs as a proportion of jobs) 2008-2013



Notes: Northern Ireland has been excluded as an outlier on the basis that it saw a decline in the self-employment rate over the period in question.

Source: Labour Force Survey, ONS and Workforce Jobs, ONS.

The regional story appears to add to a picture in which self-employment is growing as an alternative to unemployment when employee jobs are less of an option.

One possible explanation for the increasing numbers moving from unemployment to self-employment is that recent policy changes that encourage unemployed people to work for themselves have had an effect in recent years. These have been the subject of some discussion – with the New Enterprise Allowance, the Work Programme, and the welfare benefits cap all suggested as potential drivers. It is not possible to drill down to the precise impact of each of these initiatives, but the information we do have suggests that none of them are likely to have made a large contribution to the overall growth of self-employment:

- The **New Enterprise Allowance (NEA)** has offered a pathway for unemployed people to become self-employed via a loan, a weekly allowance and mentoring support between April 2011 and the end of 2013. 40,000 people had started receiving the allowance, or around 3,500 per quarter, compared to total quarterly in-flows to self-employment of 280,000 over the same period. A recent evaluation of a sample of these participants found that 78 per cent stayed off out-of-work benefits for a year. As the authors of the analysis note, it is not possible to conclude from this that all of those 78 per cent remained self-employed for that period: they may have found work as an employee or had a change in family circumstances making them inactive. Just looking at NEA starts in comparison to in-flows to self-employment from unemployment (for the period that the data overlaps) suggests that people on the NEA scheme account for a maximum of 4 per cent of moves from unemployment into self-employment over the period, or 1 per cent of all people starting out as self-employed. And this is without accounting for the fact that some people on the NEA would have moved into self-employment anyway if the scheme hadn't existed, and so can't properly be counted as part of its net impact. In sum then, although the NEA is

likely to have been critical to some individuals making the leap into self-employment, its impact on the overall self-employment growth is likely to have been minimal.

- The impact of the government's flagship welfare-to-work scheme, the **Work Programme**, is particularly hard to discern because information is not published on how many of the 250,000 sustained jobs achieved by the programme up to the end of 2013 were self-employed. Some media coverage has suggested that this scheme in particular is encouraging participants to consider self-employment; however, we have no data on what percentage of the quarter of a million job outcomes produced by the programme are self-employed.²² In addition, although the Work Programme is broader than previous initiatives, it is the latest in a succession of outcome-funded, welfare-to-work programmes that have supported the long-term unemployed into employment for more than a decade. In this context, it is unlikely that the *additional* impact of the Work Programme has played a significant role in recent self-employment growth.
- Finally, there has been some suggestion that the overall **benefit cap** introduced in late summer 2013 may have contributed to the most recent uptick in self-employment, with households registering as self-employed in order to claim tax credits and cease being affected by the cap. This theory was raised at the Bank of England's most recent Monetary Policy Committee meeting.²³ However evidence for any sizable effect seems thin on the ground: 38,600 households had their benefits reduced by the cap, and in a recent piece of DWP research on the impact of the policy, only 9 per cent of respondents were found to be in work (although the research did note that most of these were working part-time and / or self-employed).²⁴

Taken together then, there does not seem to be a convincing case that supply-side labour market policies have been a significant driver of the growth in self-employment in recent years.

Why are the self-employed staying longer?

As we have seen, more than a quarter of the overall growth in self-employment is nothing to do with new self-employed people, and simply down to people staying self-employed for longer, and this decline in the number leaving self-employment has not been observed to nearly the same extent for employees. What, then is happening?

Our view is that two main factors are likely to be at play:

- The decline in people leaving self-employment is likely to be partly **a function of an expanding and ageing workforce**, with the raising of the retirement age and longer life expectancies driving people to remain in employment for longer. Since, as we saw in the previous chapter, self-employed people are older than employees, this structural shift in the workforce is likely to have a much larger effect on the self-

²² Barnes, H. (2013) "Work advisers 'pushing jobless into self-employment'", BBC, 3 February 2013

²³ Bank of England (2014) "Minutes of the Monetary Policy Committee Meeting, 9 April 2014"

²⁴ <https://www.gov.uk/government/publications/benefit-cap-post-implementation-effects-headline-findings>

employed. In support of this argument, there is some evidence that self-employment is increasingly an option that allows older people to keep earning but work less: the growth in part-time working among the self-employed discussed in the previous chapter has been particularly concentrated among the over 60s. **Over half (51 per cent) of self-employed people aged 60 and over now work part-time, up from 46 per cent in 2005, while the equivalent figures for employees aged 60 and over have been falling.** Looked at the other way round, almost a third (32 per cent) of part-time self-employed people are now aged 60 and over, compared to just 13 per cent of part-time employees. As the Bank of England's Monetary Policy Committee recently hypothesised, self-employment seems to be growing as an alternative to retirement.²⁵

- In addition, the **qualitative differences between self-employment and employee jobs** can hold down the out-flow rate from self-employment during tough economic periods (as the years immediately following the crisis were). Because of the minimum requirements of employee contracts and relevant legislation, particularly around hours and minimum wage levels, a consequence of a challenging economic climate for businesses will be an increase in redundancies. By contrast, self-employed people may respond much more elastically, running down their hours and/ or earnings but sticking with self-employment, particularly if their view is that they are unlikely to be better off trying to switch to an employee job, or moving into unemployment or economic inactivity. The hours, desired hours, earnings and attitudes of self-employed people will provide further indications as to whether such elastic behaviour is taking place and its implications for self-employed people and the economy. Subsequent sections will explore these in detail.


Summary

This chapter has broken down the headline growth in self-employment during the recovery into its component parts: the rise in people becoming self-employed, which we estimate accounts for nearly three quarters (72 per cent) of the overall growth, and the decline in those leaving self-employment, which we estimate account for the remaining quarter (28 per cent).

What about the likely longevity of current self-employment levels? There are clearly signs that the recession has played its part in self-employment growth. Unemployment, coupled with low employee vacancy levels, can reasonably be assumed to have become a greater push factor, and some of the self-employed who might previously have become employees may well look for opportunities to work for someone else again as vacancies re-emerge. In addition, the ability of the self-employed to be more elastic around low demand and a constrained economic environment than businesses with employees is likely to have contributed to the decline in the rate at which people leave self-employment.

However, that's not the whole story. The declining rate of self-employment leavers may have as much, if not more, to do with an ageing and expanding workforce and self-employment being used as an alternative to retirement. And beyond a growth in part-time working it is

²⁵ Bank of England (2014) "Minutes of the Monetary Policy Committee Meeting, 9 April 2014"



hard to find any change in the type of people becoming self-employed, and the industries and occupations they move into, pre- and post-recession. With respect to those who enter and leave self-employment, both cyclical and structural factors seem to have played a part. Therefore, while we are unlikely to continue to see increases on the scale of the post-recession period in coming years, it is reasonable to assume that high levels of self-employment within the workforce are here to stay.

Life as a self-employed person

The previous sections of this report have discussed the characteristics of the self-employed and how they have changed since the recession. But, excluding the higher proportion of self-employed people working part-time, these figures tell us little about how much self-employed people are working and whether they would like more or fewer hours.

A linked issue is earnings: we can see that the overall profile of the self-employed hasn't shifted hugely, but have their earnings followed the same pattern? And how does being self-employed actually affect your ability to access basic financial products? Given that the self-employed are not included in the roll-out of auto-enrolment pensions, to what extent are they likely to be vulnerable in later life? This chapter will attempt to answer these questions.

Underemployment

On most factors, the self-employed do not look significantly different since the recession, or if they do, a similar trend is present for employees. One notable exception is part-time self-employment. Between 2005 and 2013, the share of self-employment accounted for by people working part-time grew by 22 per cent while only a 4 per cent increase was seen among employees.

What has driven this growth in self-employed people working part-time? There are a number of potential explanations, all of which may have played a role. For instance, there is a possibility that this reflects the labour market preferences of the group, especially given that other changes have included a higher proportion of women becoming self-employed, as well as a higher proportion of workers of retirement age. Another interpretation would be that more of the self-employed have become part-time due to a constraint on the amount of work they are able to get. While it is difficult to get at the labour market preferences of self-employed people, the latter hypothesis can be tested by looking at their level of underemployment, that is, whether they want to work more hours.

Underemployment is not a straightforward concept to measure. For instance, an increase in reported underemployment may not reflect a deficit of hours worked so much as a fall in earnings per hour and hence a desire to work more hours to compensate. As discussed in the previous chapter, the self-employed are able to respond more elastically to a drop in demand, for example by lowering the rate charged to their clients. The minutes of the April meeting of the Monetary Policy Committee report that "survey evidence suggested that the self-employed were only slightly more likely to be looking for another job than were employees."²⁶ While this is a useful point of comparison, what exactly "another job" entails for an employee or a self-employed person may vary. An employee who was unhappy in their current role due to insufficient hours would most likely look for another position if they could not easily extend the number of hours they currently work. For self-employed people however, the relationship is less straightforward. You may well be happy in your status as a self-employed person but nonetheless feel you would like more business than you have.²⁷

²⁶ Bank of England (2014) "Minutes of the Monetary Policy Committee Meeting, 9 April 2014"

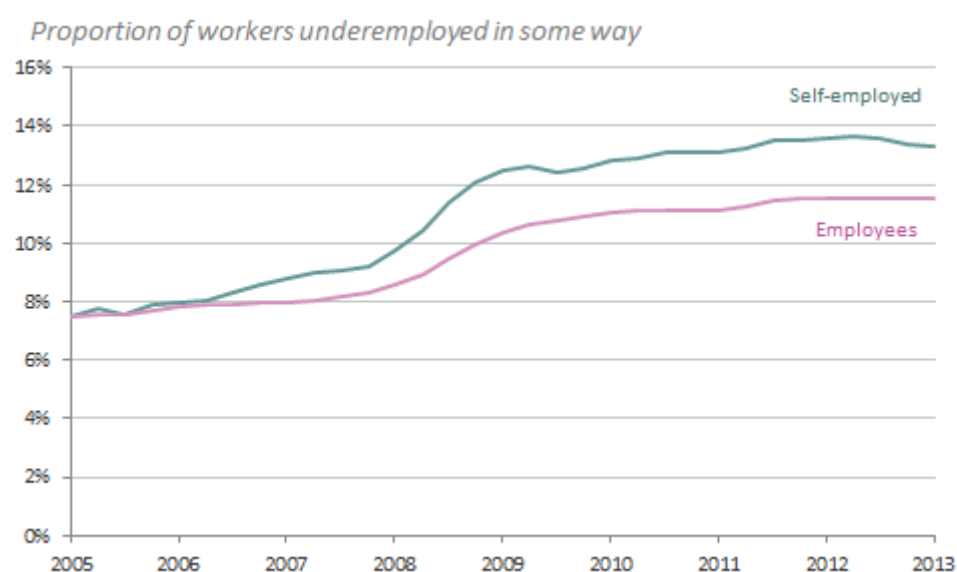
²⁷ Another difficulty with the underemployment reporting of the self-employed is that it is hard to differentiate between hours spent trying to generate business and hours actually carrying out work. Both of course will be necessary in any business but the ratio of time spent trying to find work, to time spent doing work is likely to

To try and respond to some of these difficulties, Figure X shows the proportion who are seeking:

- a different job to get longer hours;
- an additional job; or
- more hours in their current job (but who aren't looking for a new job).

Taken together, this should give us a sense of the size of the workforce seeking extra work. As Figure 16 shows, the share of self-employed people and employees who are underemployed using this definition looked very similar in 2005 and 2006. From 2007 onwards, the percentage of underemployed among the self-employed rose, with employees following in 2008. The rates for both groups have remained stable from 2010 to 2013 but the small gap that opened up between the self-employed and employees has remained.

Figure 16: Underemployment rate of the self-employed and employees



Notes: Four-quarter rolling average, with horizontal axis showing mid-points of averages.

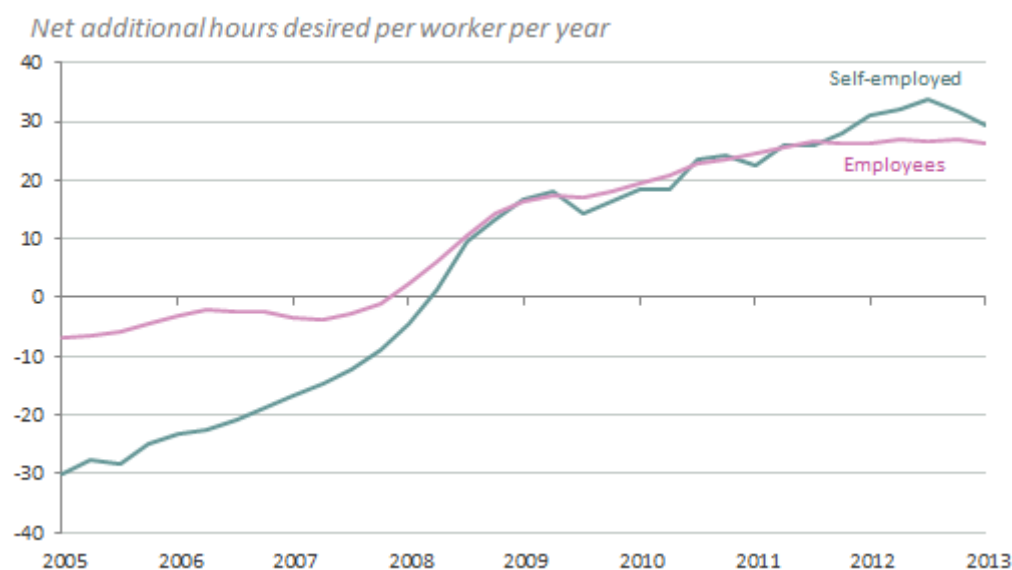
Source: Labour Force Survey, ONS.

This suggests that self-employed people are slightly more likely to be underemployed than employees. What this doesn't reveal is the *intensity* of the underemployment i.e. how many additional hours are employees and self-employed people seeking? Building on the Bell and Blanchflower underemployment index, we analyse the extent to which the self-employed are underemployed by aggregating the number of additional hours of work (at the same rate of pay) that underemployed people would like, less the number of hours by which overemployed people would like to reduce their working time.²⁸ Looking at this figure per self-employed person or employee gives a measure of the extent of underemployment within each employment type and allows us to assess how closely the experience of self-employed people matches that of employees. As Figure 17 reveals, it would now appear that underemployment is slightly higher among the self-employed than employees.

increase during a downturn. Whether someone who spends 35 hours a week calling potential clients and five hours a week working would say they desire more hours is debatable and likely to vary from person to person.

²⁸ The index is described in Bell, D.N.F and Blanchflower, D.G. (2013) "Underemployment in the UK revisited" National Institute Economic Review, No. 224 May.

Figure 17: Levels of underemployment among the self-employed and employees



Notes: Four-quarter rolling average, with horizontal axis showing mid-points of averages.

Source: Labour Force Survey, ONS.

While the figure for the self-employed is not considerably higher than for employees, it is a noteworthy change compared to eight years ago: in 2005, the self-employed were highly overemployed, much more so than employees. If the 2005 picture represents the norm for self-employed people, the current comparable levels of underemployment between the self-employed and employees entail much more slack among the self-employed than the economy has been accustomed to dealing with.

Our analysis of underemployment leads us to conclude that while the spare capacity among the self-employed is not greatly higher than employees, we have seen more of a shift among the self-employed on this measure. A related question is therefore whether self-employment is a first choice: do the self-employed prefer to be their own boss or was it a choice made due to the lack of employee vacancies?

First choice or last resort?

Respondents to our survey were asked whether today, taking everything into account, they would prefer to be self-employed or an employee. The great majority of the self-employed report a preference for being self-employed. Excluding those who answered “don’t know”, more than eight out of ten (83 per cent) of self-employed people reported that being self-employed is their preference. Nonetheless, that leaves nearly one in five (17 per cent) of self-employed people who would rather be an employee.

Interestingly, a divide is visible when we look at those who have become self-employed since the recession – respondents who answered they became self-employed in the last five years – compared with the more established self-employed. Among the new entrants, 28 per cent report they would prefer to be an employee, compared with just one in ten (11 per cent) of the longer-standing self-employed. This may tell us something about the difficult conditions facing those who became self-employed in the past five years, forced to do so due to an inability to find work as an employee. Alternatively, it may reflect the fact that new entrants are always more likely to want to be employees, given they may be struggling to establish

and grow their business, compared with the longstanding self-employed from whose ranks those who were poorly suited to self-employment have already fallen away. A lack of genuine options regardless of when they became self-employed appears to be a greater problem for people in semi- and unskilled roles, among whom a quarter would prefer to work for someone else, compared to more than 1 in 8 (14 per cent) in higher-skilled roles.²⁹

Our survey also asked respondents why they originally became self-employed: was it due to a lack of better work alternatives, solely out of personal preference or a combination of both? For the vast majority (84 per cent), becoming self-employed is a choice taken, at least in part, out of personal preference. However, just over a quarter (27 per cent) of the newly self-employed say they became self-employed due to a lack of better work alternatives, falling to 10 per cent among those who have been self-employed for five years or more. This lends support to the argument that for a significant minority of the newly self-employed, the shift to becoming their own boss was taken out of necessity rather than preference.

Earnings

The fall in the earnings of employees has been well-documented. Between 2008 and 2013, employees at the median saw their earnings drop by more than 5 per cent, although that figure conceals a range of experiences, with men and workers in their twenties and thirties faring particularly badly.³⁰ What is less understood is how the earnings of self-employed people have been affected since the downturn. This is primarily because the various surveys of earnings – including the Labour Force Survey, the Annual Survey of Hours and Earnings and Average Weekly Earnings – do not capture the self-employed. This means that other, less timely datasets (principally the Family Resources Survey) have to be relied upon, meaning that our knowledge of how self-employed people's earnings are developing runs a year or more behind that of employees.³¹

Even within those datasets that do capture self-employed earnings, challenges remain. It is often argued that the ease and incentive to conceal earnings is greater for the self-employed. This means that the size of the “grey economy” (unreported earnings) is an important factor in interpreting earnings patterns.³² Research conducted for Morgan Stanley estimates that the size of the grey economy may have increased by as much as 4 or 5 per cent of GDP since the start of the recession, due to a combination of factors including higher VAT rates and excise taxes, changes to the benefits system and limited employee vacancies.³³ As that research acknowledges, attempting to put a figure on the size of the grey economy is a highly uncertain process.

²⁹ The analysis for skill level is done by grouping those reporting they worked in “Admin and Service Occupations” and “Process and Elementary Occupations” into semi- or unskilled, with the remaining categories classed as higher-skilled.

³⁰ All earnings in this chapter are adjusted using RPI-J inflation.

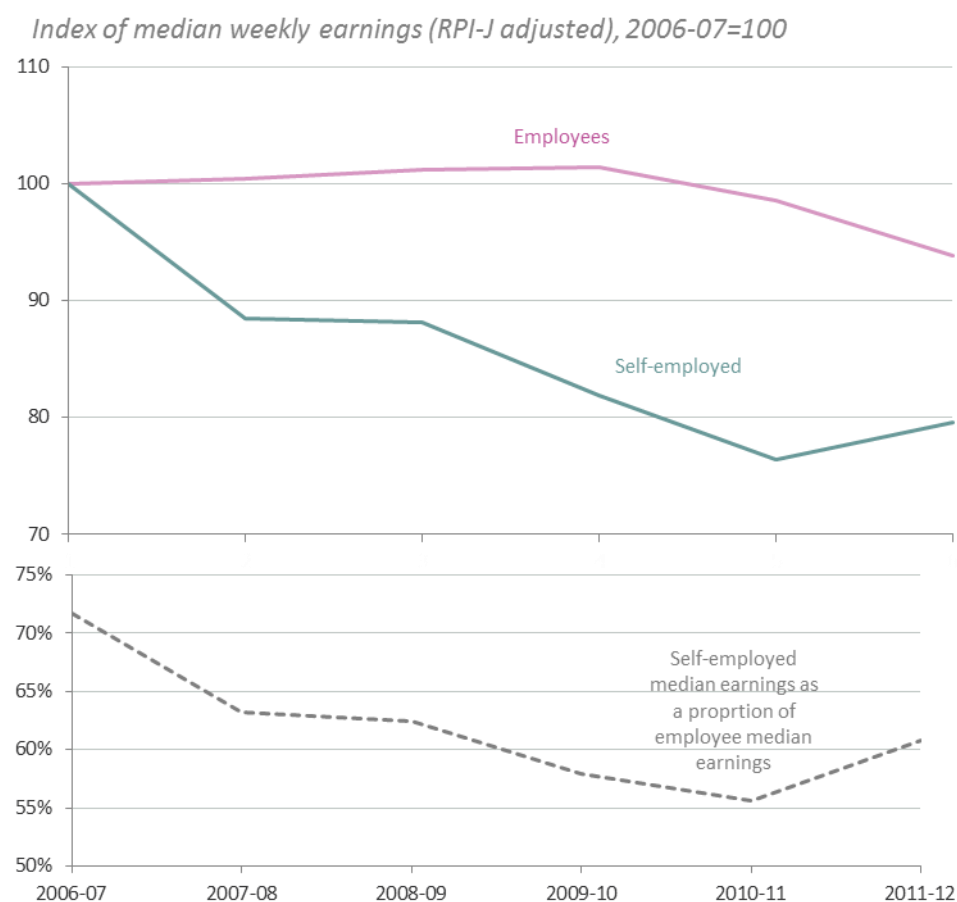
³¹ Additional data on the incomes of the self-employed are published by HMRC in the Survey of Personal Incomes. However, the inclusion of people for whom self-employment makes up only a small proportion of their total income, along with the use of fixed income bands in which the data are reported, means that our analysis has chosen to focus on the Family Resources Survey.

³² One potential way of testing the reliability of the reported earnings of the self-employed is to compare their consumption patterns with those of employees. Studies suggest that when spending rather than income is considered, the self-employed look much more like employees. This lends support to the theory of under- or miss-reporting of earnings by the self-employed. See for example Brewer, M. (2014) “Why are households that report the lowest incomes so well-off? Measuring living standards with income and consumption”

³³ Ashworth et al. (2014)

Our analysis of the Family Resources Survey (FRS) finds the weekly earnings of typical self-employed people appear to have been hit far harder than those of employees, who themselves have experienced unprecedented falls. In 2011-12, the earnings of the median self-employed worker were 20 per cent lower than in 2006-07. Over the same period, employee earnings fell by 6 per cent. As Figure 18 shows, self-employed earnings were already falling in 2006-07 and continued to do so until 2010-11. This differs from the experience of employees at the median, where earnings were flat between 2006-07 and 2009-10 before falling. As a result of these trends, the typical self-employed person earned 40 per cent less than the typical employed person in 2011-12; in 2006-07, the gap was 28 per cent.

Figure 18: A comparison of the earnings of employees and the self-employed



Source: Family Resources Survey, ONS.

What should we make of this relative collapse in median self-employed earnings? One possible explanation concerns the ability of the self-employed to respond more flexibly to low demand. Employee earnings may have held up during the crisis years as many employees lost jobs and were taken out of earnings altogether (and so did not drag down the median), whereas, as we have seen, the self-employed have the flexibility to stay put and make do with less. The slight bounce in median self-employed earnings in 2011-12 would seem reasonable in this context, as the earnings of those who had stuck around began to pick up after a few years of struggle.

A second, but related, factor concerns the hours that people are working. We have seen that part-time working has grown faster for the self-employed in recent years – has this dragged

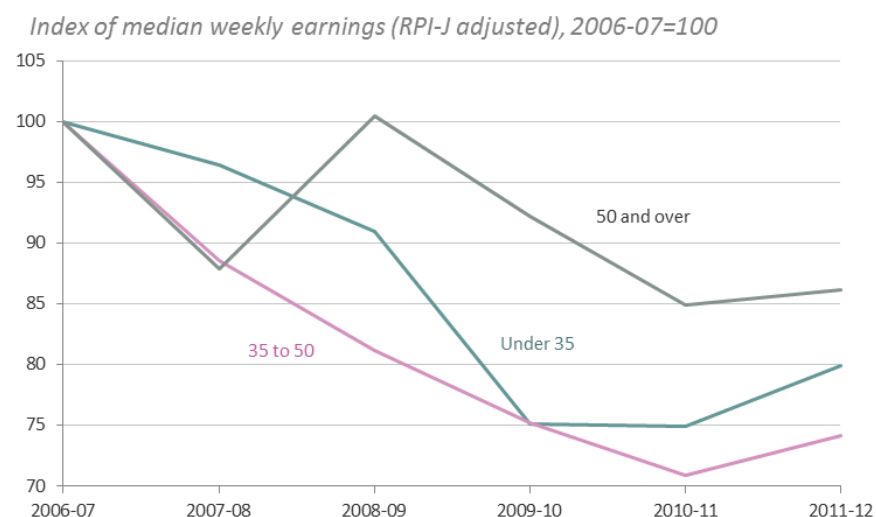
on median weekly earnings? There is some evidence that this has acted as a drag on earnings. The earnings decrease is slightly smaller when looking just at the full-time self-employed, or just at the part-time self-employed, which suggests that part of the earnings collapse relates to a growing tendency among the self-employed to work fewer hours. However, even when isolating our analysis to full-time workers there remains a clear distinction between the self-employed and employees: earnings of full-time self-employed people fell 18 per cent between 2006-07 and 2011-12, compared to just 5 per cent for full-time employees. Of course, changes in the precise number of hours *within* the full-time group may further explain the relative difference.

Finally, other changes in the composition of self-employed workers – towards lower-paying sectors or within lower-paid age groups, for example – might explain the relatively large decline in self-employed earnings since 2006-07. We know that those aged over 50 (whose earnings are below average) have been growing as a share of the self-employed, although they have also been growing among employees. And we know that women (whose earnings are lower than men's) now make up more of the self-employed than they did in 2006-07, while female employee levels have been flat. In terms of sectors, we have seen that self-employment has grown strongly in both higher-paying sectors, such as real estate and business activities, and lower-paying ones, such as health and social work. The picture looks mixed, but it is likely that the changing composition of the self-employed workforce explains some of the median earnings collapse.

Acknowledging the fact that changes in the composition of the self-employed *across* groups may explain some of the overall earnings decline, it is useful to explore what has happened to earnings *within* these various groups? Broadly speaking, median self-employed weekly earnings have fallen across the board, and to similar extents. As with employees, the earnings of women have fallen less than those of men but the gap between the two is nowhere near as large: among employees, female earnings have only fallen by 40 per cent of the fall in male earnings; among the self-employed, the fall in female earnings is equivalent to 81 per cent of the decrease among men. And as we have seen, the fall has occurred to similar extents for full-time and part-time workers, a drop of 18 per cent vs. 14 per cent respectively.

One personal characteristic where the fall has been less uniform, and differs from that experienced by employees, is age. Among employees, those in their twenties were worst affected. When looking at the self-employed, it is people of prime earning age – 35 to 50 years old – who have experienced the steepest decline, though the fall has been only slightly milder for other age bands. For the typical self-employed worker in this group, whom you would expect to be at peak earning capacity, earnings have fallen by more than a quarter (26 per cent) since 2006-07.

Figure 19: Change in the earnings of the self-employed by age

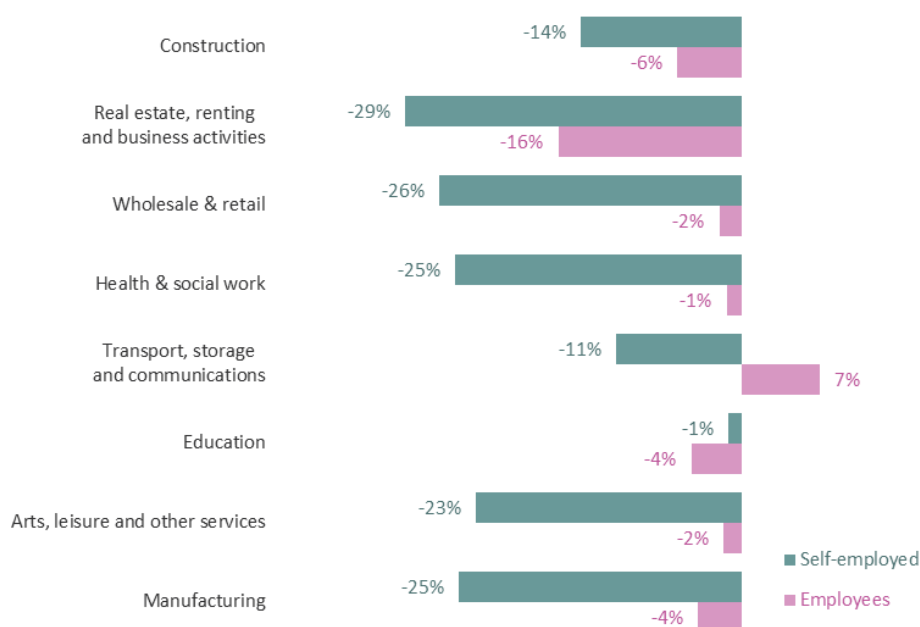


Source: Family Resources Survey, ONS.

Focusing just on full-time workers, self-employed earnings have fallen further than employee earnings in the vast majority of industries. Figure 20 underlines that although some variation is seen – large falls in some sectors contrasted with much smaller drops in others – median earnings have fallen across the board. Barring education, the drop in the earnings of the self-employed has been greater in every sector than that of employees.³⁴

Figure 20: Change in the median full-time earnings of self-employed and employees by industry

Change in full-time median weekly earnings, 2006-07 - 2011-12 (RPI-J adjusted)



Notes: Industries with fewer than 200,000 self-employed jobs are excluded from this chart. The older SIC 1992 industrial classification is used here, as SIC 2007 is not available over the time-periods compared.

Source: Family Resources Survey, ONS.

³⁴ The resilience of the earnings of the self-employed in the education sector may be explained by the high proportion of supply teachers who are classed as self-employed but whose wages will be set by local authorities and thus less likely to drop suddenly as demand remains relatively constant.

As discussed above, one important limitation of data on self-employed earnings is that it is far less timely than data from other sources that exclude the self-employed, and the trends discussed above do not capture the sharpest periods of self-employment growth in the past couple of years. What might have happened to the earnings of the self-employed since 2011-12? The survey conducted by Ipsos MORI asked respondents whether their earnings had risen, fallen or stayed the same in 2012-13 compared to the previous financial year. Half of respondents (51 per cent) said their income had stayed the same with a quarter (25 per cent) reporting their earnings had gone up and a quarter (25 per cent) saying they had gone down.³⁵ While this excludes people who refused the question or responded “don’t know”, it does appear that for most self-employed people, their earnings in 2012-13 were about the same, with equal numbers experiencing rises and falls. Although we know nothing about the scale of the increases and decreases, this limited picture gives no indication that a substantial turnaround in self-employed earnings has occurred.

Resources and security

We have seen how the earnings of self-employed people have fallen since the recession, with the hit being felt relatively evenly. This tells us how their income from self-employment has been affected but less about their ability to access products and services. Concerns have been expressed about the extent to which self-employed people are covered by pensions, have savings and are dealing with debt.³⁶ This section presents an overview of how the self-employed compare with employees on these matters and the extent to which the trend has altered pre- and post-recession.

Access to personal credit and housing

As discussed, the incomes of the self-employed can be unpredictable and lumpy. This means that proving their ability to pay rent and to meet regular repayments on credit or mortgages can be challenging. While this analysis of course acknowledges that agreements should not be drawn up when there is a strong likelihood of the debtor being unable to meet the requirements, it should nonetheless be of concern if self-employed people experience such problems *primarily due to being self-employed*.

Our Ipsos MORI survey finds that 15 per cent of self-employed people who tried to obtain personal credit or loans say they have been prevented from doing so because of their employment status, as illustrated in Figure 21.³⁷ A similar pattern is seen when looking at housing, whether it is securing a tenancy or being approved for a mortgage. One in five (20 per cent) of self-employed people were prevented from getting a mortgage due to being self-employed. The difficulties faced by self-employed people in accessing loans and mortgages are echoed in the Bank of England’s NMG survey, which suggests that these difficulties exist for the self-employed to a greater extent than for employees.³⁸ Finally, although affecting a

³⁵ Percentages do not sum to 100 due to rounding.

³⁶ http://www.citizensadvice.org.uk/index/pressoffice/press_index/press_20140319.htm

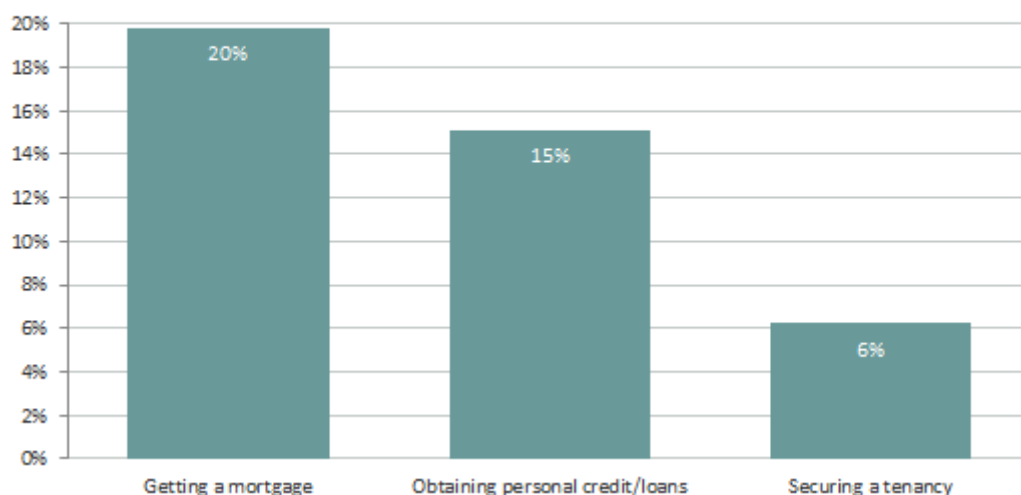
³⁷ In any survey evidence, we are reliant on individuals’ perception of why they had difficulties and whether it was because they were self-employed – for example from the lender’s perspective they may actually have been refused because they had an irregular income or couldn’t provide sufficient evidence of their income, rather than directly because they were self-employed.

³⁸ Caution should be exercised when comparing the questions asked in the Ipsos MORI survey to those in the NMG survey. The NMG survey conducted for the Bank of England finds that 44% of self-employed people who applied for

smaller group, 6 per cent of the self-employed experienced difficulty in securing a rental tenancy due to being self-employed.

Figure 21: The difficulties experienced by self-employed people in accessing credit and housing

Proportion responding yes when asked "Has being self-employed ever prevented you from..."



Notes: Base figures exclude those responding "not applicable" or "don't know": Getting a mortgage, N=616; Obtaining personal credit/loans, N=672; Securing a tenancy, N=499.

Source: Resolution Foundation analysis of Ipsos MORI survey data.

The landscape in this area has been reshaped in recent weeks by the Mortgage Market Review (MMR), which has sought to improve the workings of the system for lenders and borrowers. The new rules call for tighter affordability checks before a mortgage can be advanced, switching the liability for the verification of the potential borrower's income from the individual to the lender. Because income among the self-employed can often prove irregular, such workers are likely to find it more difficult to get a mortgage under this new regime. Indeed, the Council of Mortgage Lenders has stated that it finds it "difficult to determine how lenders will be able to continue to lend to [self-employed] borrowers in these circumstances."³⁹

And this problem might extend to existing self-employed mortgagors too. Those wishing to re-mortgage at the end of the existing deal may find their options for restructuring limited, leaving them stranded on the Standard Variable Rate applied by their current provider – with little protection as to the level that rate might reach. The MMR attempts to reduce such risks by including a provision for side-stepping some of the affordability rules for existing borrowers, but there is no guarantee that lenders will be willing to offer new deals. A

a loan over the past year (2012-13) were refused or were unable to borrow as much as they would have liked, compared to 22% of employees. Similarly, 24% of self-employed people (who weren't already homeowners) reported that they were unable to obtain a mortgage due to their personal circumstances compared to only 5% of employees in the NMG. Both reported differences from the NMG are significant at the 5% level. While the gap between the self-employed and employees points in a similar direction to the findings of our survey with Ipsos MORI, the questions are not directly comparable as the NMG question asks whether "personal circumstances" rather than being self-employed were a factor.

³⁹ Council of Mortgage Lenders, (2012) "Mortgage Market Review: Proposed package of reforms, Response by the Council of Mortgage Lenders to the Financial Services Authority Consultation Paper CP11/31".

forthcoming Resolution Foundation report on debt and mortgages will address these issues – and possible solutions – in more detail.

Financial security

While the dip in the earnings of the self-employed has been proportionally larger than that for employees, it does appear that the earnings of the self-employed are slightly more likely to be supplemented by income from another member of the household. Among the self-employed, 30 per cent are the sole earner in a couple household compared to 35 per cent of employees in couple families. This has not changed in recent years.

Savings are another important buffer against fluctuating earnings. One in three self-employed people surveyed by Ipsos MORI said they were “not very confident” or “not confident at all” that they knew how much they would earn next year. When it comes to savings, the self-employed look very similar to employees. In 16 per cent of families in which the main earner is self-employed, their total savings are less than £1,500, compared with 15 per cent of families in which the main earner is an employee. Again, there was little change in this proportion between 2005-06 and 2011-12. This does not mean that the self-employed are not of concern; for those families with little savings, be they employees or self-employed, dealing with unexpected costs with little financial security is tough.

Self-employed people have traditionally been less likely to be a member of a personal pension scheme, missing out on offers to employees. Our analysis of the Family Resources Survey highlights a chronic lack of pension saving. Only 30 per cent of self-employed people have any kind of personal pension, compared with 52 per cent of employees (either individually or via their employer). This has not changed in recent years (2005-6–2011-12). This is supported by our Ipsos MORI survey, in which just 34 per cent of self-employed respondents said they were currently contributing to a personal pension. Perhaps more concerning is that the figure for self-employed people aged 60 and over was only slightly higher, at 39 per cent.

Data drawn from another ONS survey suggest this trend has worsened over recent years.⁴⁰ Breaking the self-employed down by gender, women are less likely to have a current personal pension than men (20 per cent vs. 34 per cent) and the majority of women have never had a personal pension (60 per cent, compared with 46 per cent of men). While self-employed men are more likely to be covered than women, recent decades have seen a particularly steep fall for full-time self-employed men: between 1998 and 2011, the proportion with a current personal pension decreased from just under two in three to one in three (64 per cent to 34 per cent) while the number who had never been a member of such a scheme rose from 27 per cent to 46 per cent.

An argument can be made that self-employed people may be able to sell their business upon retirement to allow them to finance their later years and so pensions are of less importance. While this may be true for some, it is difficult to gauge how many people this might apply to and the value of those businesses. Moreover, the reverse scenario could also apply, in which

⁴⁰ Data is drawn from the 2011 General Lifestyle Survey produced by the ONS. A personal pension is defined to include personal pensions (which may include SIPP), stakeholder pensions and retirement annuities.

self-employed people choose to re-mortgage their homes or liquidate their assets in order to fund their business, and may not recover all of this value upon retirement.⁴¹

An area where the government has taken a positive step to improve the pension savings of the self-employed is in its introduction of the Single-Tier State Pension. From 2016, it will bring the self-employed fully into the state pension, treating their National Insurance contributions the same as employee contributions for state pension purposes. But the roll out of auto-enrolment for employees looks set to widen the gap in pensions savings between the self-employed and employees.

Summary

Underemployment among the self-employed has increased above that for employees. Beyond the number of hours they are working, most self-employed people are happy with their current employment status. The picture is slightly muddled, however, by the quarter of those who became self-employed since the recession who did so due to lack of better alternatives and a similar proportion who say they would prefer to be an employee. This suggests that the strong headline self-employment figures do hide a level of spare capacity but not to the extent feared by some.

On earnings, self-employed people have experienced a chronic fall, with earnings decreases felt across the board. In other respects, the self-employed do not appear to be in a much worse position than employees. The proportion of self-employed people who have low levels of savings is not dissimilar to that of employees. But given that the self-employed are more likely to have problems accessing personal credit and loans to help smooth their consumption patterns and maintain their living standards when times are tough, their picture looks somewhat more challenging.

⁴¹ Indeed, anecdotal evidence indicates that self-employed people are increasingly intermingling their personal and business finances.

Conclusion

Our analysis suggests that those who argue that the surge in self-employment is wholly structural or cyclical offer only a partial explanation of the recent trend, with clear evidence for the presence of both. Our analysis reveals a much more varied picture, with three key points emerging:


Structural factors are clearly at work. The workforce as a whole is growing, which explains the rapid increase in the number of people who are self-employed and the notable but relatively slower growth of the share of total employment that is self-employment. For a growing group of older workers, it appears that self-employment has become an alternative or complement to retirement. Those who became self-employed post-financial crisis are not markedly different from those who were already self-employed and where changes in the characteristics of the self-employed have occurred, these have largely been mirrored among employees. Significantly, the growth in self-employment pre-dated the downturn.

However, an **important part of the growth of self-employment has been due to cyclical factors.** A greater share of people who leave unemployment have moved into self-employment since the recession than previously. Self-employment seems to have played differing roles across the country, with no growth in employees since 2008 in the majority of regions while the number of self-employed has risen everywhere other than Northern Ireland. The proportion of the self-employed who work part-time has risen from 23 per cent to 28 per cent since 2005, twice as large as the shift among employees and the earnings of the self-employed have fallen more drastically than those of employees. Underemployment among the self-employed looks to be marginally worse than for employees, both in the proportion of the group who are seeking to increase their hours and the number of additional hours they are seeking. That desire for more work and/or higher earnings appears to be echoed in our survey: a significant minority of the self-employed, particularly those who have become self-employed in the past five years, say they would prefer to be an employee and became self-employed due to a lack of better work alternatives.

Third, **one in seven workers in the UK are now self-employed.** Many of that group are experiencing problems accessing basic services and products. There is always a need for caution when talking about making it easier for people to access mortgages but taken together with difficulties obtaining personal credit and loans and securing a rented property, it seems this growing portion of the UK's workforce could be better served. Also of great concern is the high proportion of self-employed people who report they do not contribute to any kind of pension. Although the introduction of the single-tier pension system in 2016 should improve the protection of the self-employed in later life, in other areas of financial security it is the self-employed **group who would benefit from more attention.**

In combination, the evidence that the self-employed are more likely than employees to want more hours and the rising share of the self-employed working part-time points towards some slack remaining hidden beneath the strong employment and unemployment figures. How this picture develops over coming months and years will therefore be an important consideration in debates over when interest rates should start to rise.

In this context, the fact that the earnings of the self-employed have never been included in the key metrics which give us a sense of the strength of the economy is now a significant

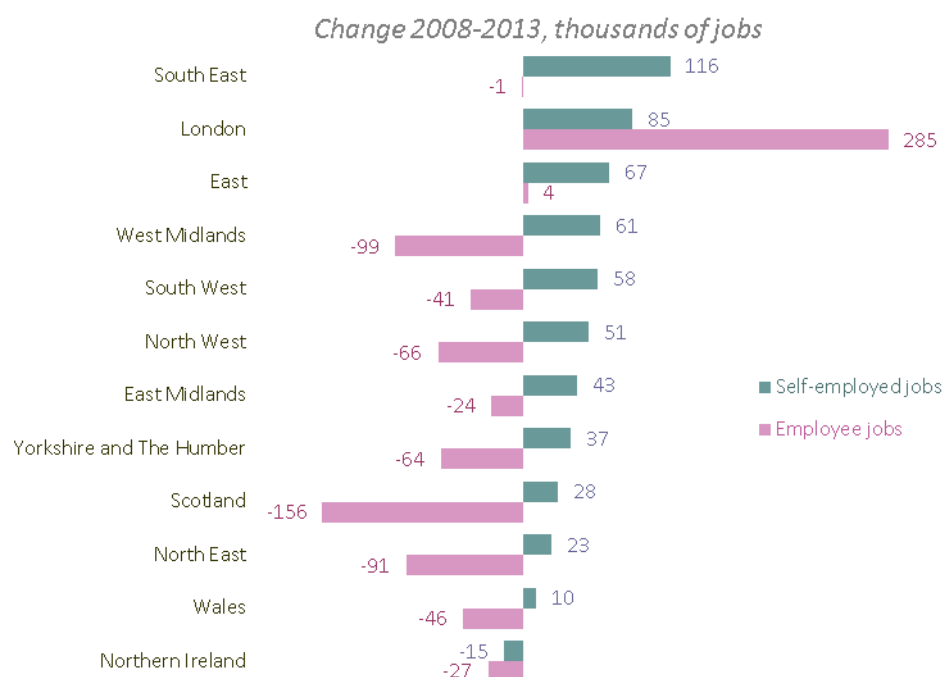


limitation to the timeliness of our economic understanding. As the self-employed become a larger part of the workforce, so too will the importance of their absence from this data. The fact that many of the key debates on the health of the labour market are now referencing the self-employed makes this all the more of an omission. As our analysis has shown, in some parts of the UK all of the net growth in employment has been due to the self-employed. Overlooking this group means our ability to judge the experiences of households and the health of the economy is limited.

Annex

This annex provides supplementary figures to this report. Figures A1 and A2 provide further information on the regional breakdown of self-employment growth. Figure A1 shows changes in the number of self-employed and employee jobs – rather than workers – within regions since the start of the recession, and Figure A2 shows changes in the number of employees and self-employed people since the overall employment recovery began in early 2010.

Figure A1: Changes in regional self-employed and employee jobs since 2008



Source: Workforce Jobs, ONS.

Figure A2: Changes in regional self-employment and employees during employment recovery phase

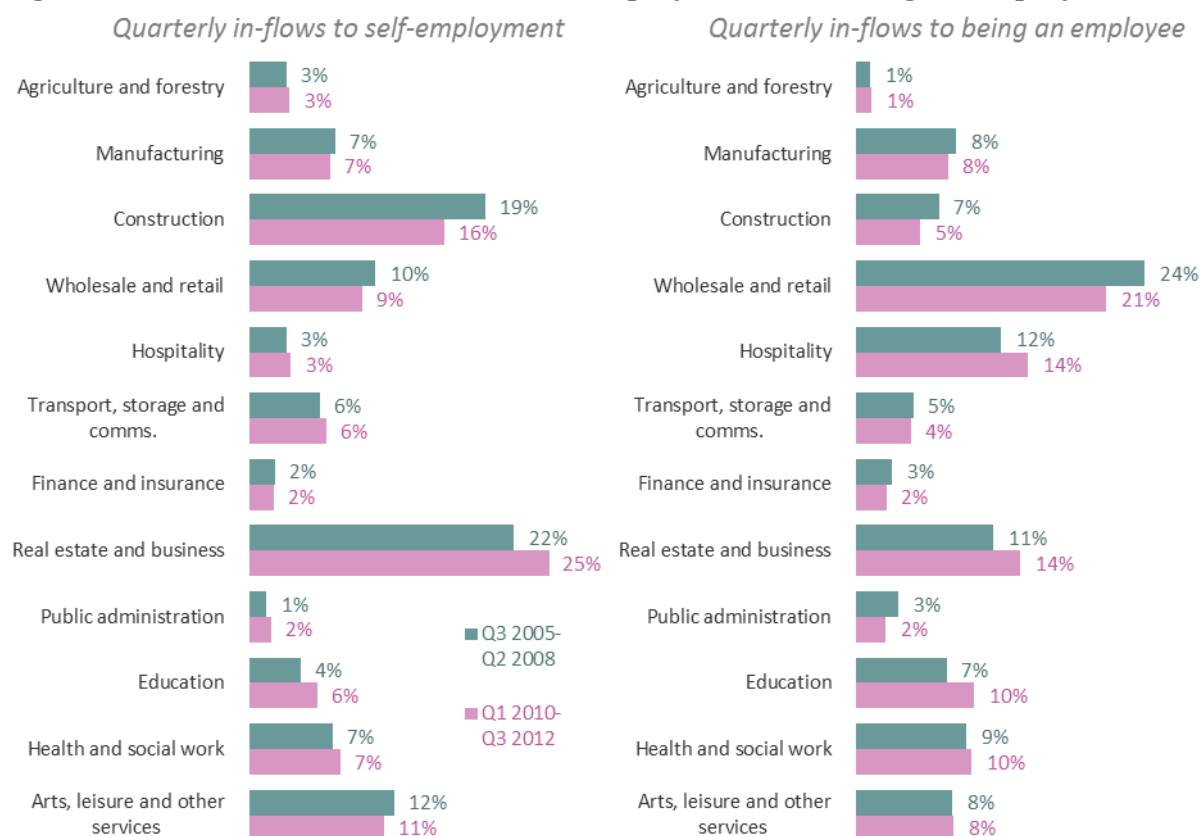
Change during employment recovery phase (Q2 2009-Q1 2010 average - 2013 average (latest)), thousands of workers



Source: Annual Population Survey, ONS.

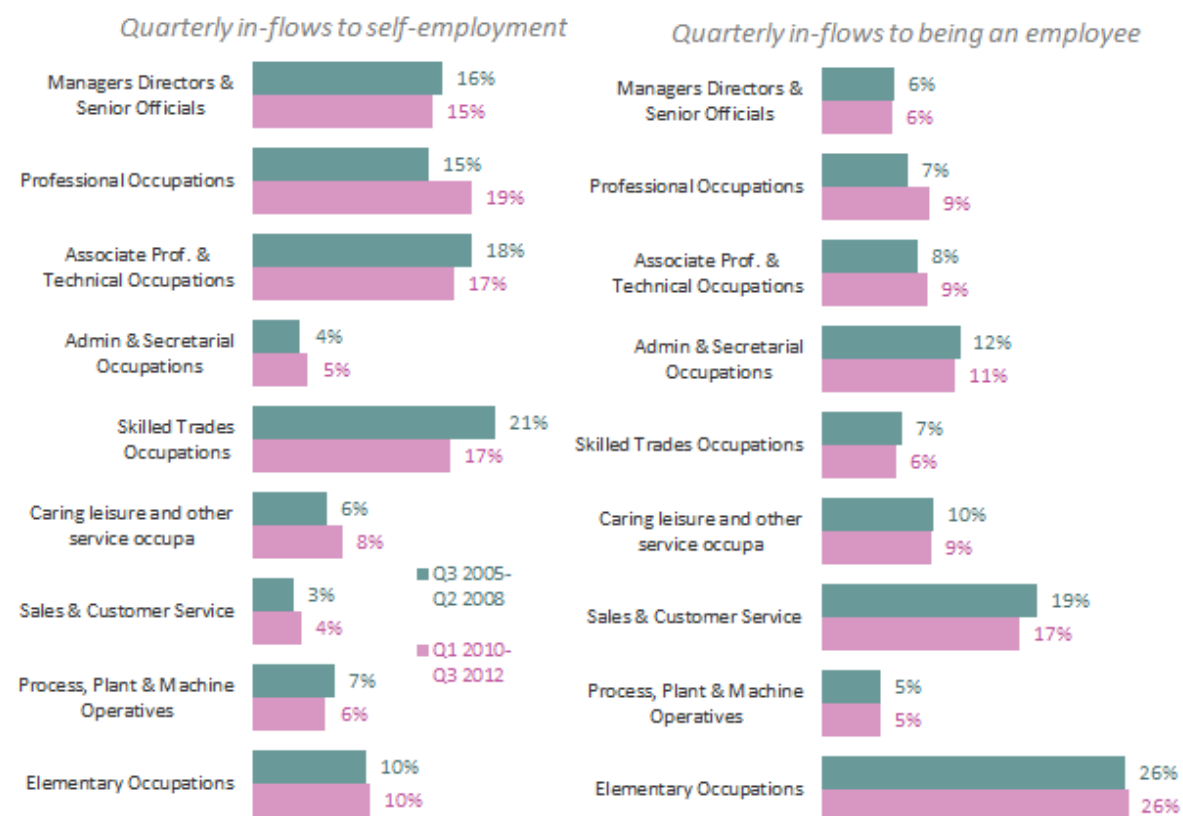
Figures A3 and A4 provide further information on the characteristics of new self-employed people in recent years. Specifically, the two Figures compare the in-flows to self-employment and employee jobs, before and after the recession, in terms of the industries (A3) and occupations (A4) that individuals moved into. Neither profile has changed very much when comparing the period after the recession to the period before, and those industries and occupations where self-employment in-flows have increased have generally also experienced increases in employee in-flows.

Figure A3: Industries of in-flows to self-employment and being an employee



Notes: The older SIC 1992 industrial classification is used here, as SIC 2007 is not available over the time-periods compared.
Source: Two-Quarter Longitudinal Labour Force Survey, ONS.

Figure A4: Occupations of in-flows to self-employment and being an employee



Source: Two-Quarter Longitudinal Labour Force Survey, ONS.

The Resolution Foundation

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- developing practical and effective policy proposals; and
- engaging with policy makers and stakeholders to influence decision-making and bring about change.

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