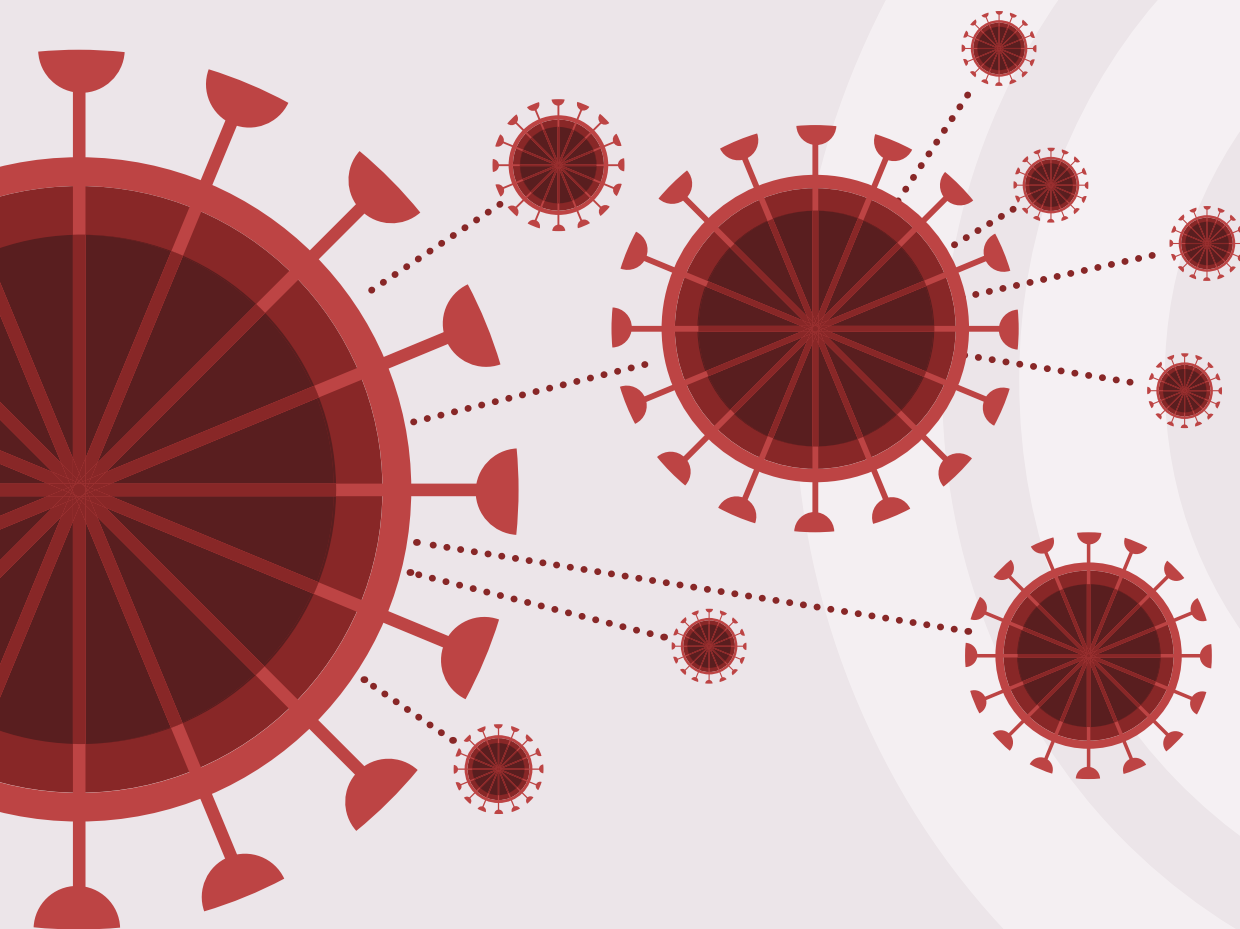


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From Covid-19 to collapse? The self-employed and the cost of living crisis

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From Covid-19 to collapse? - the self-employed and the cost of living crisis

CEP COVID-19 ANALYSIS

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February 2023

Summary

- The sixth LSE-CEP survey of the self-employed was undertaken in November 2022, following five previous surveys in May 2020, September 2020, February 2021, September 2021 and May 2022.
- This latest survey finds that the downward trend in income levels of the self-employed reported in May 2022 has continued. This persistence reiterates concerns over the financial problems experienced by the self-employed. On the intensive margin, there is a faint recovery in the hours worked, but this remains below pre-pandemic levels.
- The cost of living crisis is hitting small businesses particularly hard, with the increase in energy prices and other input costs compounding the effects of the Covid-19 pandemic. Inflation has taken over as the most significant challenge that the self-employed have to overcome. Their incomes, like that of employees, are falling sharply in real terms.
- One of the main concerns facing the self-employed is their relatively low levels of pension provision. Almost three quarters do not make contributions to a personal pension scheme, expecting to rely instead on the basic state pension only, or other forms of income. A lack of sufficient liquidity is reported to be the main reason for the absence of additional retirement savings.
- We explore the possibility of a scheme that would help overcome this pensions gap. The analysis shows that the self-employed would be willing to contribute up to five per cent of their earnings, providing there is a government bonus contribution of three per cent, into a hypothetical scheme. This willingness varies by levels of income: almost half of the self-employed with annual incomes typically above £10,000 and a third of those with lower incomes would contribute under these conditions.
- The new socio-economic composition of the self-employed and disquiet with the UK political context have combined to generate changes in voting attitudes. The results suggest a shift in allegiance towards Labour (38 per cent) away from the Conservatives (24 per cent), their traditional party of choice. A significant proportion (16 per cent) said that they would not vote.
- One of the characteristics of the self-employed has been their ability to sustain their activities even in difficult economic conditions. However, the series of shocks encountered over the past three years is fully testing this resilience. We have already observed a recent exodus of the self-employed. This analysis suggests that the exodus will continue, even among the most robust enterprises, given the scale of challenges.

Introduction

After two very trying years for the economy, the last nine months have seen the UK endure new downturns. Post-pandemic peaks in the demand for goods and energy, combined with the disruption caused by the Ukrainian conflict, have caused inflation to hit a 40-year high. Although inflation has, at least for now, stopped rising, prices in December 2022 were about double their values the previous year, with the highest growth rate observed for the energy and food sectors (ONS, 2023a; ONS, 2023b). As lower income households tend to consume more of these goods, the effective inflation rate is 30 per cent higher for the poorest tenth of households, compared to wealthiest tenth (Resolution Foundation, 2022), further exacerbating inequalities. The self-employed too keep being negatively affected. They were pessimistic at the start of the year with only 17 per cent of SMEs planning to grow in 2023 (ACCA, 2023). and feel left behind by the government, whose support towards the cost of energy will significantly decrease in the spring.

This report is the sixth policy brief from the Centre of Economic Performance (CEP) that analyses the condition of the self-employed in the post-Covid economic context and the newly emerging challenges. (Blundell and Machin, 2020; Blundell et al, 2020, 2021; Blackburn at all, 2021; Blackburn at al., 2022). With the Covid-19 threat giving way to record high inflation and the cost of living crisis, the results of this survey show how little a breathing space they have had to recover from the recent hits. As official statistics illustrate a continuing drop in the number of self-employed, most of those who have remained in the sector keep suffering falling incomes and profits, while experiencing marginal improvements in work levels. And, as their resources are absorbed by the rising prices of energy and business costs, these persistent financial difficulties make them unable to adequately save for retirement.

The sixth round of the LSE-CEP Survey of UK Self-employment collected responses from over 1,500 people in self-employment¹ between 17 and 29 November 2022. The survey questions investigate the main labour market outcomes such as income, profits and hours worked, both at the time of collection and in the previous year, the main challenges currently faced by the self-employed, expectations for the future, and basic demographics. In this latest round, we have added a section on pensions, to look into how the self-employed prepare for their retirement. We complement this data by drawing upon the Labour Force Survey (LFS), whose most recent wave we use to weight survey results and make them representative, as well as on HRMC's (2022) statistics on private pensions memberships. Additional details on how the data were collected are provided in Appendix B.

Incomes of the self-employed are in the doldrums

The past six months have been very challenging for the UK economy. This has been especially the case for the self-employed. The Covid-19 crisis has given way to new and persistent difficulties, both for workers and businesses. In this context, the long-awaited recovery for the self-employed is yet to materialise. The self-employed have been consistently affected by the economic downturns the UK has experienced since March 2020 (Blundell and Machin, 2020; Blundell et al., 2020, 2021; Blackburn at al., 2021; Blackburn at al., 2022), and continue to report falls in their income. Figure 1 shows how the most recent reported income distributions

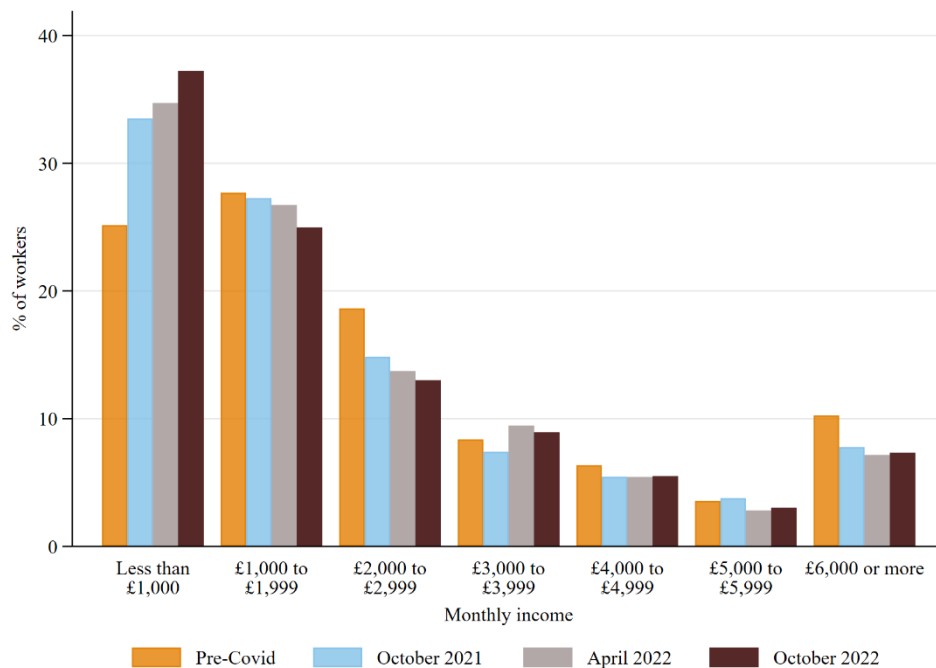
¹ Of these, about 1375 were still self-employed at the time of the survey, while the rest has survived the panel selection due to outdated records. See Appendix B for more details on the analysis sample.

compare with previous months. The share of self-employed reporting income levels in the lowest income bracket shows no sign of falling but, in fact, seems to be rising. This is reflected in the low proportion of respondents in the highest income group, which remain lower than pre-pandemic. The same pattern is observable for profits (Figure A1 in Appendix A).

Once again, the results from our survey highlight how the fall in income has translated into significant financial difficulties for the self-employed. In October 2022, the share of the self-employed who were having trouble paying for basic expenses rose by two percentage points over previous levels. It is likely that this fall in income has been compounded by the ongoing cost of living crisis, which has hit the lowest income households hardest (IFS, 2022). These households include a significant share of (especially solo) self-employed workers.

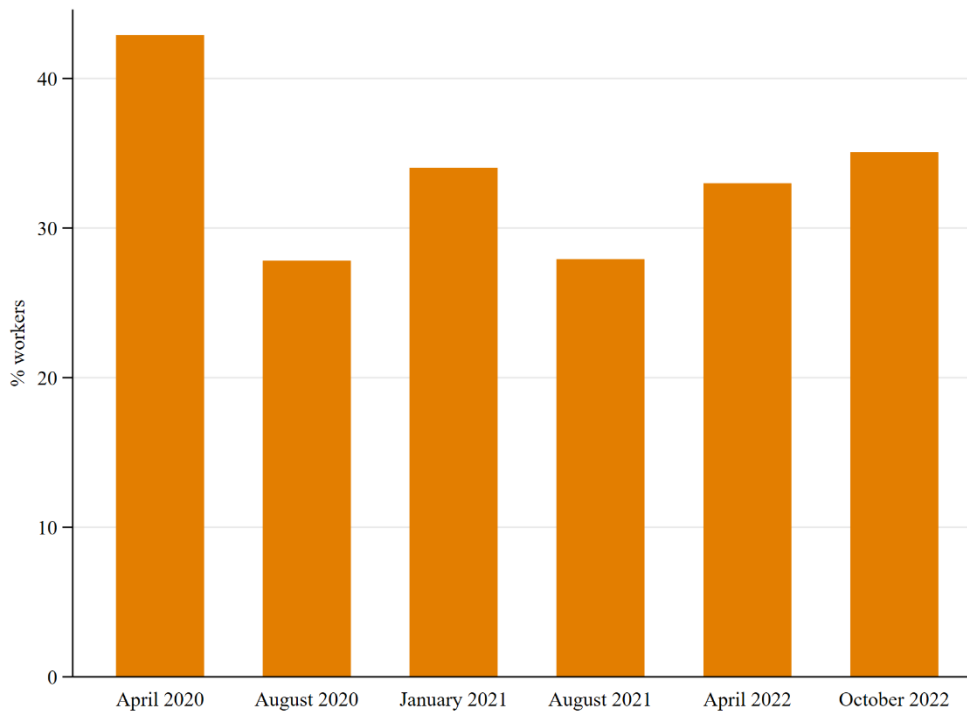
The fall in income reflects the proportion of the self-employed reporting less work in October 2022 than usual for that time of year. The share of workers reporting a fall in hours has decreased by almost 15 per cent since our May survey, but still represents 35 per cent of self-employed. Figure A2 in Appendix A confirms this trend with a partial recovery of weekly hours worked with respect to a year ago, although still far from pre-Covid levels. Moreover, as “working for oneself” has not regained its pre-Covid levels of attraction, entries into self-employment remain low. Data from the Office for National Statistics (ONS) (2023c) show that the numbers in self-employment remain below those at the beginning of 2020, by more than three-quarters of a million, and the largest fall has been in the number of full-time self-employed (more than 730,000).

Figure 1: Monthly incomes – Pre-Covid, October 2021, April 2022, October 2022



Source: LSE-CEP Survey of UK Self-employment November 2022.

Figure 2: Share experiencing financial difficulties



Source: LSE-CEP Survey of UK Self-employment May 2020, September 2020, February 2021, September 2021, May 2022 and November 2022.

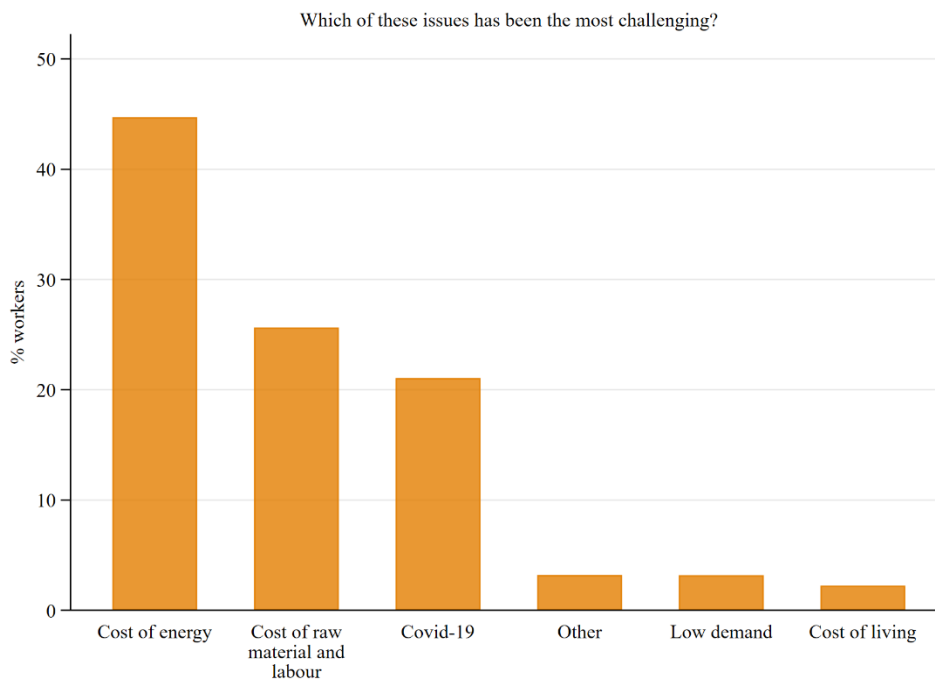
Rising costs remain the main concern of the self-employed

Since spring 2022, although the dangers from Covid-19 have become less salient, the self-employed are facing new challenges in their day-to-day lives. In particular, the soaring cost of energy, boosted by the inflationary impact of the ongoing conflict in Ukraine, has deeply affected households and businesses. Our new data confirms previous survey findings (Blackburn et al, 2022b), energy prices are now the leading issue for the self-employed, followed by the price of raw materials and labour, and then the impacts of Covid-19 (Figure 3).

A report by the Federation of Small Business (FSB, 2022a) highlights the critical relevance of this issue for small businesses. Its survey reports extremely high levels of concern (96 per cent) about energy prices among small firms, with the greatest share of extremely concerned owners working in the food and accommodation sectors (68 per cent). This should not come as a surprise, given that 63 per cent of small business report increases in their energy expenses, with 44 per cent having doubled or more their energy costs (FSB, 2022b).

The plan by the government to cut energy costs through the Energy Bill Discount Scheme, starting from April 2023, has been received with disappointment from the business sector. This is not surprising as it will replace the more generous Energy Bill Relief Scheme (EBRS), in place until March, and is likely to place many small firms in financial jeopardy. In November 2022, when interviewed about their future prospects should EBRS come to an end, 24 per cent of small businesses said they would downsize, close or radically change their business model (FSB, 2022b).

Figure 3: Issues affecting the self-employed



Source: LSE-CEP Survey of UK Self-employment November 2022

Saving for pensions is a luxury for some self-employed

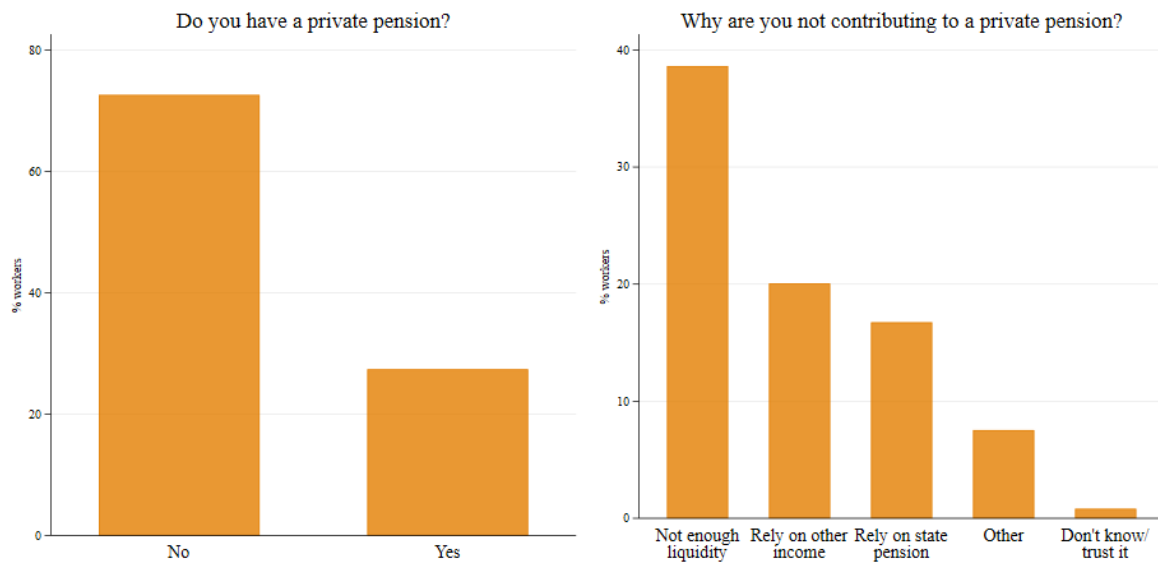
One of the perennial challenges facing self-employed individuals is the ability to match the employer-provided benefits that are usually available to employees working in organisations, particularly those in salaried employment. In the UK, all workers paying national insurance contributions gain the right to a basic state pension (currently £185.15 per week, equivalent to just more than £9,600 per year when contributing for 30 qualifying years). On top of this most employees² receive a workplace pension, ie a pension scheme arranged by the employer to which the employee also pays in and the employer usually also contributes. This system is, by definition, unavailable to the self-employed who, in the absence of an “employer”, are expected to take care of their retirement income themselves. According to the OECD (2021), this means that self-employed on average receive pensions that are 44 per cent the amount received by employees.

The most common instrument to accrue an additional pension in the UK is to contribute to a private personal pension scheme. In our survey, we asked the self-employed whether they are contributing to a private personal pension. The first panel in Figure 4 shows that the vast majority of self-employed (73 per cent) do not currently pay into additional pensions. When asked the reasons for not contributing, lack of liquidity seems to be predominant, highlighting once again the scarcity of resources affecting many self-employed. Table A1 in Appendix A displays the results of a regression model that investigates the characteristics of those that do

² According to the ONS (2022a) 80 per cent of all UK employees had workplace pensions in 2021.

not contribute to a private pension. Keeping income constant, this is likely to be solo self-employed and those that have entered self-employment more recently. The fact that those who do not own their house are also less likely to be enrolled in a private pension scheme reinforces the connection with their lower incomes and economic status.

Figure 4: Self-employed and private pensions

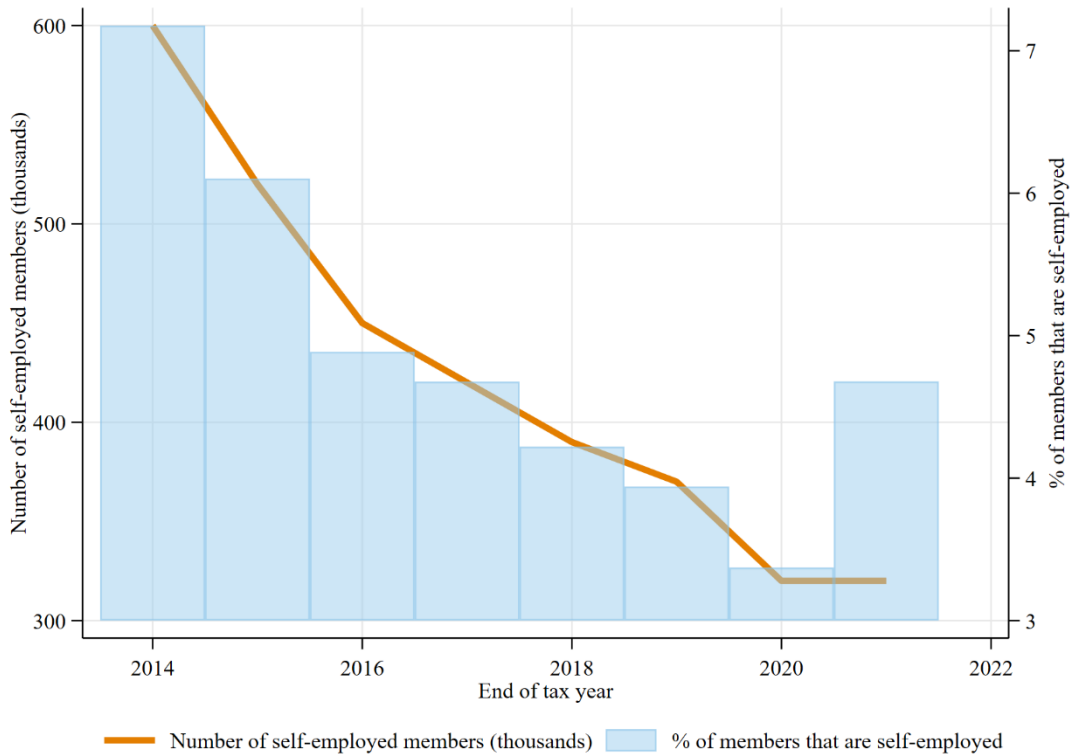


Source: LSE-CEP Survey of UK Self-employment November 2022

The lack of private pension savings among the self-employed represents an additional margin of inequality in comparison with workers in salaried employment. Figure 5 illustrates how both the number and the share of members of private pensions that are self-employed have decreased in the last few years³. The drop does not reflect a general trend in the number of self-employed: a recent report by the Fabian Society (Harrop, 2022) reveals rather a more profound change in their savings habits, which predates the recent crisis. In sum, the proportion of self-employed contributing towards a pension fell from 48 per cent to 16 per cent between 1998 and 2018. The same report advocates for an additional pension, to be paid to the self-employed through a government contribution that would be roughly equivalent to the tax relief on employers' contributions. Such an initiative, it is argued, would help mitigate the unequal access to and take up of private pension schemes between the self-employed and salaried employees. Undoubtedly, this differential is a combination of the absence of pension scheme that provides sufficiently attractive returns on investment for the self-employed and a reflection of their relatively low- and precarious-income levels.

³ The increase in the share in 2021, compared to the previous three years, was driven by a drop in the number of employees' memberships.

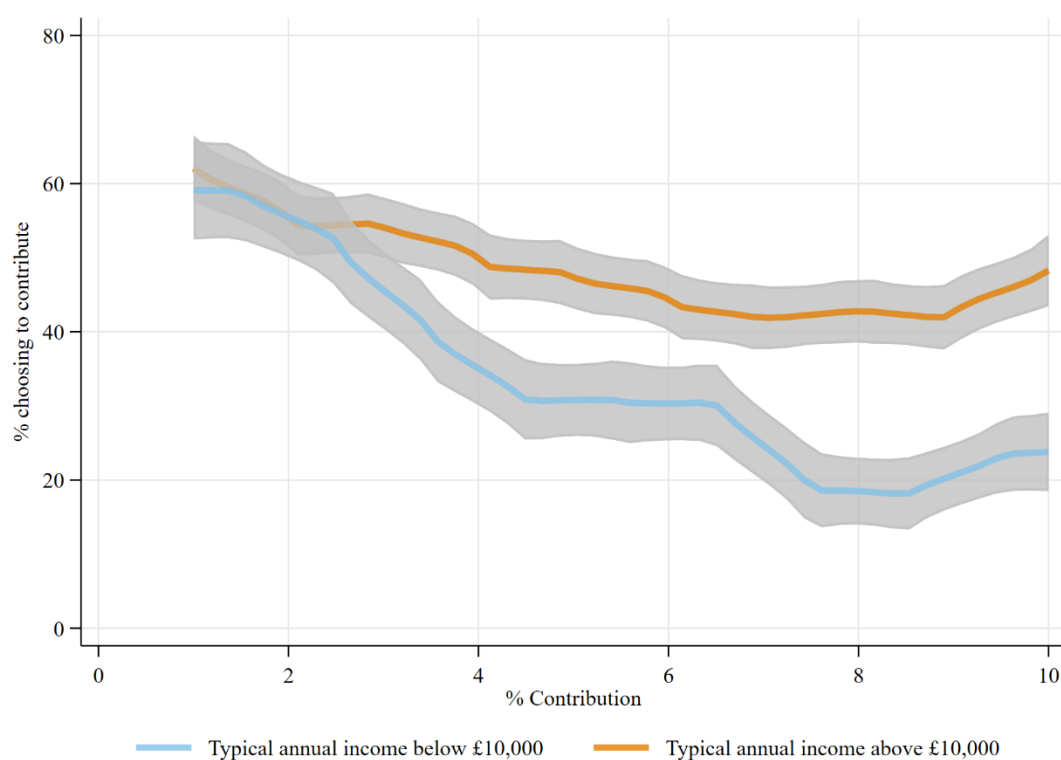
Figure 5: Members of private pensions



Source: HMRC Private pension statistics 2022

In order to explore the willingness and ability of the self-employed to pay into a different type of pension scheme system made available to them, we test the feasibility of a pension scheme that works on similar principles to those available to salaried employees. This would involve an additional state pension to be paid to the self-employed through a government contribution that would be roughly equivalent to the tax relief on employers' contributions. Harrop et al. (2022) for example, propose a scheme in which the self-employed would contribute with at least five per cent of their earnings, matched by the government at a rate of three per cent of earnings. The bonus would be available to self-employed earning below £10,000, as for the rest of these workers the new digital tax reporting planned from April 2024 may pave the way for the introduction of pension contributions requirements.

Figure 6: Willingness to pay for additional state pension



Source: LSE-CEP Survey of UK Self-employment November 2022

In our latest survey, we test this proposal by eliciting the willingness of self-employed workers to pay for an additional state pension, at different personal contribution rates, keeping constant a state contribution of three per cent of earnings. Figure 6 plots the resulting demand curves by income group. The vertical axis shows the percentage willing to contribute, and the horizontal axis the percentage of their income they are willing to sacrifice. Our results show that around one third of low-income self-employed would take up the scheme at the proposed rate of five per cent, and almost 50 per cent of the group with a typical income of over £10,000 would sign up for such scheme. In general, as the proposed contribution rises, demand for additional pension remains high among the latter group, while it decreases for those on lower incomes. This differential reflects the impact of liquidity constraints and the precariousness of some of those in self-employment. Hence, such an initiative would be welcomed by some of those in self-employment but would not be a cure-all for a pensions crisis among those in self-employment.

A wind of change is blowing through UK politics

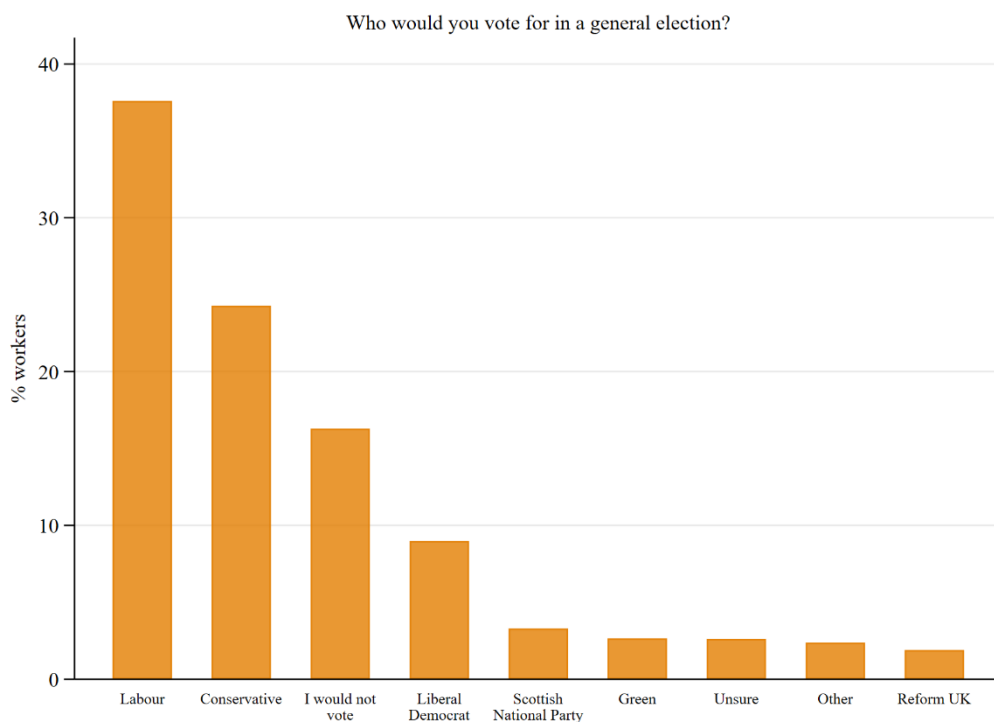
The recent economic events and the changes to the number and composition of the self-employed in the UK have brought with them political significance. The self-employed have always been a heterogeneous group, consisting of people of different ages, with different motivations and ambitions, operating in a range of business sectors and occupational groups and with variations in income levels. How this socio-economic diversity is reflected in their political views and voting intentions has attracted attention over many decades (Scase and

Goffee, 1981). Historically, the self-employed and small businesses have tended to vote for Conservative and centrist parties, as the parties of free enterprise that represent the interests of enterprise and business (Barisione and De Luca, D, 2018; Scase and Goffee, 1991). However, evidence elsewhere that has focused on the self-employed suggests that there has been a change in their attitudes and this allegiance is over-simplified if not misrepresented (Jansen, 2017). This, it is argued, is a result of changes in the composition of the self-employed as well as that of the political parties seeking to support this growing working population.

Within the UK there have also been specific short-term factors that may also have affected voting intentions. Changes in the leadership of the Conservative party and the unstable economic climate have led to changes in the voting intentions of the population as a whole and a decline in confidence in the government. Political poll results collected by the website Politico (2023) show that since the beginning of the Covid crisis in March 2020 there has been a decrease of more than 50 per cent in support for the Conservatives to 22 per cent, while Labour’s support increased to 52 per cent in October 2022. However, given the loyalty of the self-employed to centrist and right-wing political parties, to what extent has there been a shift in the attitudes of the self-employed?

Our analysis shows that the self-employed are more likely to vote Labour than any other party if there was a general election: 38 per cent compared with 24 per cent Conservative (Figure 6 November 2022). A significant proportion (16 per cent) would choose “not to vote” probably reflecting their disaffection with politicians and / or apathy.

Figure 7: Political views of the self-employed



Source: LSE-CEP Survey of UK Self-employment November 2022

We use our survey data to investigate what particular enterprise and personal characteristics of the self-employed correlate with political behaviour, using some simple linear regression. The results (in Table A3 in Appendix A) show that those self-employed workers who are more likely to report being “worse off” as a result of the crisis (when including government support) are 11 percentage points *more likely* to vote Labour. Younger people who are self-employed are also *more likely* to support Labour, but less so if they became self-employed in the last year. But we also find that the young, solo self-employed would be *less likely* to vote in a general election (Table A2 in Appendix A).

Whether or not the results of the survey will be actually translated into real votes remains to be seen but they confirm a longer-term, structural shift, reflecting changes in the composition of the self-employed population, irrespective of any immediate political party crises (Jensen, 2017). The rise of the gig-economy, the precariousness of many jobs, the rise in the number of solo self-employed and the growing number of younger people in this form of employment, combine to suggest that the voting intentions will be different from those in previous decades.

Conclusion

This briefing extends our earlier analyses of the impact of the pandemic on the self-employed undertaken by CEP through to a sixth survey launched in November 2022 (Blundell and Machin, 2020; Blundell et al, 2020; 2021; Blackburn et al., 2021a; 2022). Two and a half years after the start of the Covid-19 crisis, the survey finds an ongoing crisis amongst the self-employed. The income levels of the self-employed have stalled and are still below pre-pandemic levels. The proportion of self-employed workers reporting financial difficulties has increased compared to the previous two surveys.

The challenges faced by the self-employed have become multifaceted, as the price of energy and other inputs are added to the effects of Covid-19. The increase in the cost of energy and other inputs are now reported as having more impact than Covid-19, and represent a particularly deep financial shock for the self-employed who are often operating in low-margin sectors of the economy and possess lower levels of financial reserves. Hence, the immediate outlook for the self-employed appears bleak and the reduction in support for energy bills from April 2023, further compounds this picture.

This report has also explored the perennial question of finding a suitable pension scheme for the self-employed, over and above the state pension. Evidence shows that the self-employed are less likely to have contributed to a pension scheme beyond the state pension, leading to a potential crisis on retirement (Crawford and Karjalainen, 2020; Fachinger, 2019; Harrop, 2022). Given the absence of a system that matches those available to many salaried employees, many of whom benefit from an employer contribution scheme, what sort of scheme is feasible for the self-employed? The results of our survey show that a significant proportion of the self-employed would be prepared to pay into a pension scheme that involves contributions from government. Such a scheme would help overcome the “pensions crisis” faced by many self-employed, providing them with a more equitable and secure income when they retire. Such an initiative would also help reduce the insecurity and precariousness that is often associated with being self-employed, and raise its attractiveness compared with other forms of labour-market engagement. Our sensitivity analysis shows that those on higher incomes and older self-employed workers are more likely to contribute to such a scheme, adding weight to support for consideration in policy circles. This is not surprising. Our analysis of attitudes to contributing

to a social security scheme in the previous survey also revealed differences within the self-employed (Blackburn et al., 2022).

The rise in the number of self-employed to more than 4 million people has led to recognition that they present a significant population among those eligible to vote. In investigating their voting intentions, our data found that Labour would attract more votes from the self-employed than the Conservatives. We also found a large percentage of respondents would not vote at all. These results suggest a shift from previous voting patterns - historically the Conservatives have attracted allegiance from the self-employed. Our data alone cannot explain these latest patterns. Yet they are most probably a result of a structural change in the composition of the self-employed, including changes in personal and business characteristics, and a response to short-term events, including political turmoil and the economic shocks that they have had to endure. We also find that there are differences in attitudes among the sample. Most notably younger and solo self-employed workers appear to be driving these general observations.

Overall, the survey findings make it very clear that the self-employed have faced a series of challenges over the past three years. How impactful these challenges have been, how persistent they are, and how they are processed and managed vary according to a range of characteristics. Certainly, the financial resources and resilience of the self-employed to continue in business is being particularly tested (Yue and Cowling, 2021). The plan for a reduction in support for energy bills, together with the worsening of the macro-economic climate, means that the immediate outlook for the self-employed appears bleak, especially given the drain on their financial reserves over the past three years. Looking forward, as a route to an entrepreneurial career and financial independence, the attractiveness of this type of employment is seriously under question. No one would doubt that there had been growth in self-employment prior to the pandemic and this took many forms: from those enterprises that will grow to employ others, through to independent solo-workers and part-timers. However, we are now witnessing a retreat in the number of full-time self-employed workers and those self-employed who employ others, and a rise in the share of workers at the margins of the economy: the temporary solo and part-time self-employed. This latter segment of the labour force, and the fragile position of those within it, continue to be overlooked by those who point to the tightness of the labour market in recent times. The shrinkage and shift in the composition of the self-employed represents a major crisis for the sector and the need for particular attention from policymakers. While this series of reports was initiated to analyse the impact of the Covid-19 pandemic on the self-employed, although its effects linger, this has now been superseded by a cost of living crisis.

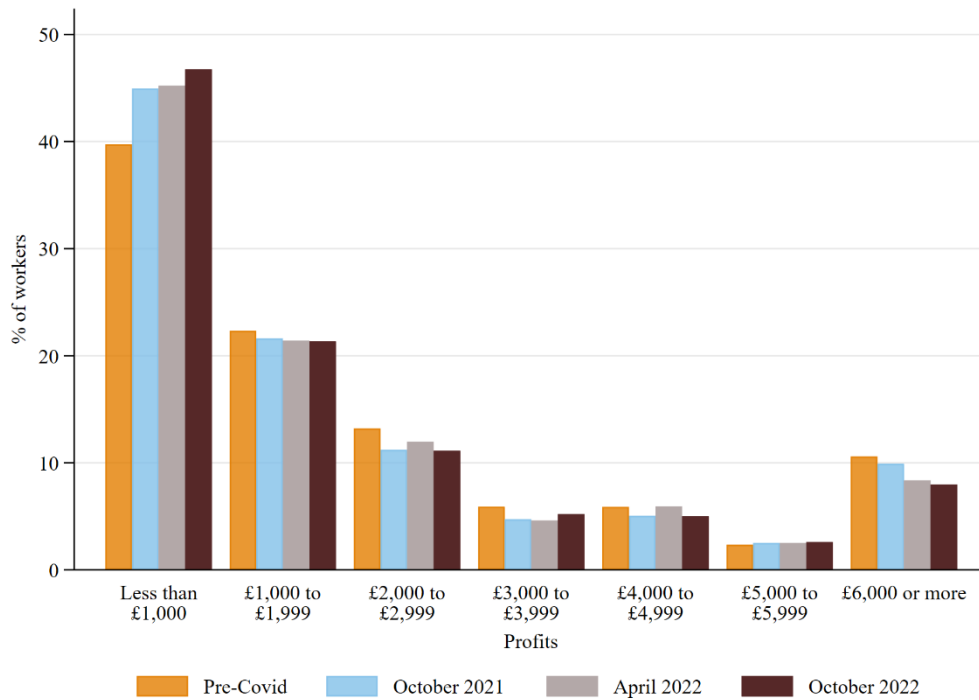
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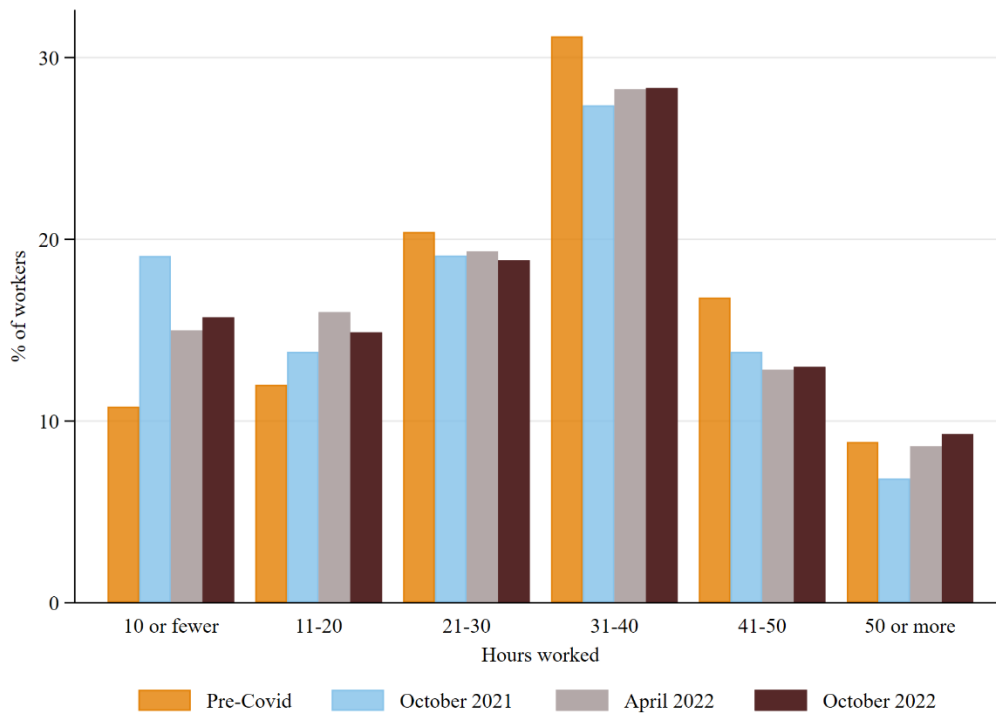
Appendix A

Figure A1: Monthly profits – Pre-Covid, October 2021, April 2022, October 2022



Source: LSE-CEP Survey of UK Self-employment November 2022.

Figure A2: Weekly hours – Pre-Covid, October 2021, April 2022, October 2022



Source: LSE-CEP Survey of UK Self-employment November 2022.

Table A1: Characteristics of self-employed with no private pensions

	Does not contribute to a private pension					
	(1)	(2)	(3)	(4)	(5)	(6)
Male	-0.023 (0.0281)	-0.012 (0.0280)	-0.010 (0.0279)	-0.033 (0.0283)	-0.020 (0.0282)	-0.009 (0.0283)
Age	-0.001 (0.0011)	-0.002 (0.0011)	0.001 (0.0013)	-0.000 (0.0011)	-0.002 (0.0012)	0.001 (0.0013)
Solo self-employed		0.162*** (0.0406)				0.140*** (0.0407)
Years in self-employment			-0.005*** (0.0019)			-0.004** (0.0018)
Owns a house				-0.113*** (0.0301)		-0.093*** (0.0301)
Risk aversion					-0.027 (0.0185)	-0.025 (0.0180)
Constant	0.964*** (0.0579)	0.820*** (0.0680)	0.905*** (0.0588)	0.980*** (0.0574)	0.978*** (0.0591)	0.818*** (0.0696)
Observations	1,410	1,410	1,410	1,410	1,410	1,410
R-squared	0.104	0.126	0.116	0.117	0.107	0.146

Notes: Robust standard errors in parenthesis. All regressions control for monthly income. Risk aversion is a coefficient calculating as in Falk et al. (2016, 2018).

Table A2: Voting behaviour of the self-employed

	Would vote in a general election					
	(1)	(2)	(3)	(4)	(5)	(6)
Male	-0.015 (0.0242)	-0.024 (0.0249)	-0.014 (0.0238)	-0.013 (0.0245)	-0.015 (0.0241)	-0.019 (0.0249)
Age	0.003*** (0.0010)	0.003*** (0.0010)	0.003*** (0.0010)	0.003*** (0.0010)	0.003*** (0.0010)	0.003*** (0.0010)
Solo self-employed		-0.067** (0.0307)				-0.076** (0.0320)
High income			-0.004 (0.0267)			-0.024 (0.0276)
Worse off after the crisis				0.013 (0.0268)		0.013 (0.0267)
Newly self-employed					-0.008 (0.0333)	-0.015 (0.0333)
Constant	0.707*** (0.0469)	0.755*** (0.0501)	0.708*** (0.0482)	0.700*** (0.0488)	0.711*** (0.0515)	0.775*** (0.0594)
Observations	1,410	1,410	1,410	1,410	1,410	1,410
R-squared	0.010	0.017	0.010	0.011	0.010	0.018

Notes: Robust standard errors in parenthesis. High income takes value of 1 if monthly income before the crisis was above £2,999. Worse off after the crisis takes value of 1 if the respondent reports to be much or somewhat worse off as a result of the crisis, including government support. Newly self-employed takes value of one if the respondent became self-employed in the last year.

Table A3: Political views of the self-employed

	Would vote Labour in a general election					
	(1)	(2)	(3)	(4)	(5)	(6)
Male	-0.091** (0.0359)	-0.077** (0.0370)	-0.077** (0.0371)	-0.075** (0.0364)	-0.092*** (0.0358)	-0.054 (0.0378)
Age	-0.006*** (0.0014)	-0.006*** (0.0014)	-0.006*** (0.0014)	-0.006*** (0.0014)	-0.006*** (0.0015)	-0.007*** (0.0014)
Solo self-employed		0.093** (0.0436)				0.071 (0.0456)
High income			-0.079** (0.0397)			-0.054 (0.0416)
Worse off after the crisis				0.106*** (0.0388)		0.110*** (0.0383)
Newly self-employed					-0.094** (0.0478)	-0.096** (0.0467)
Constant	0.784*** (0.0681)	0.722*** (0.0749)	0.817*** (0.0686)	0.731*** (0.0707)	0.842*** (0.0748)	0.764*** (0.0856)
Observations	1,167	1,167	1,167	1,167	1,167	1,167
R-squared	0.030	0.037	0.036	0.041	0.035	0.056

Notes: Robust standard errors in parenthesis. High income takes value of 1 if monthly income before the crisis was above £2,999. Worse off after the crisis takes value of 1 if the respondent reports to be much or somewhat worse off as a result of the crisis, including government support. Newly self-employed takes value of one if the respondent became self-employed in the last year.

Appendix B

The data collected for this policy brief represents the sixth wave of the LSE-CEP Survey of UK Self-employment, following the first edition in May 2020 and its follow-ups in September 2020, February 2021, September 2021 and May 2022 (Blundell & Machin, 2020; Blundell et al, 2020; Blundell et al, 2021; Blackburn et al, 2021; Blackburn et al, 2021). All data is self-reported and has been collected between 17 and 29 November. The survey was administrated by a third party, who provided the panel of individuals that have recently registered as self-employed.

Because the panel's composition is not revised daily, we were able to survey respondents that were self-employed at the time of the last update but have changed their status since. We obtained a total of 1,563 responses. The analysis uses the subset of 1,375 respondents who report their current status as self-employed. Responses are weighted to be representative of the relevant population using the aggregates from Labour Force Survey, with gender, age and education level as weighting variables. Given the current instability of the labour market, population estimates of shares are likely to become outdated relatively quickly. We have used the July-September 2022 LFS, the latest version available at the time of writing.

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The logo for the Centre for Economic Performance, featuring a stylized 'C' composed of concentric circles in shades of grey and black.

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