

Buttonwood

On their own

What explains the surge in self-employment?

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PERHAPS the future belongs to the self-employed. Steady jobs, after all, are hard to find. The

idea that a young graduate should expect to work for 40 years with the same employer until retirement seems quaintly dated.

There has been a structural shift towards self-employment on both sides of the Atlantic (see chart) as well as a cyclical one. In the fourth quarter of 2013, 90% of the new jobs created in Britain were classed as self-employment. Is the shift a sign of a thriving entrepreneurial spirit or an indicator of desperation? Are we talking Mark Zuckerberg and Facebook or Walter White and “Breaking Bad”?

Answering the question is made harder by the limitations of the data, drawn as they are from a combination of surveys, tax records and registers of company creation. Some people may incorporate as a business in order to reduce their tax bill; others may fail to report their self-employment income as a way of avoiding taxes. Some may play dual roles, having a full-time job but earning money on the side (renting out a spare room, for example). Still others may be working for their old employer as contractors, rather than for a salary.

Desperation must play a part. A paper* by Robert Fairlie of the University of California, Santa Cruz found a close link between the unemployment rate in a given American locality and the rate of new business startups. A survey by the Kauffman Foundation found that the rate of new-business creation in America declined last year, even as the economy turned up; as the report comments, there was “less pressure on individuals to start businesses out of necessity”.

Self-employment may be more socially acceptable than it used to be. Middle-class people can call themselves consultants or freelancers, rather than unemployed. The businesses they create are unlikely to be the growth engines of the future. In Britain, by far the fastest growth in recent years has been in businesses that are one-man bands.

The numbers also show self-employed Britons tend to be male, work longer hours than salaried employees and earn less. Indeed, the real wages of the self-employed fell faster than those in contractual employment between 2007 and 2012. This may help to explain why British productivity has grown only sluggishly in recent years. Setting up a new business involves a lot of time tracking down new clients or handling a host of issues (invoicing, accounting, taxes) that were previously dealt with by a company.

The new self-employed are also older. British people aged 50 and above comprised five-sixths of the increase in the category between 2008 and 2012. And there has been a rise of 160,000 in the number of self-employed people aged 65 and over since 2007. Some of that may reflect the need to replace shortfalls in pension income (a problem exacerbated by low interest rates).

But these changes are not all negative. The rise of the service economy means it is easier for

people aged 65 and over to find jobs that suit them; retirees are fitter than they would have been 40 years ago, when many had been through a long career in manual labour. Getting people to work for longer is the best way of dealing with the costs of an ageing population. In addition, a survey by the Royal Society of Arts suggests that the self-employed are happier than those in paid employment—independence counts for a lot, as does the feeling that one's work has meaning.

In the long run, this rise in self-employment will raise some interesting macroeconomic and political questions. Does it mean, as Morgan Stanley suggests in a research note, that the labour market is not as robust as it appears; that many people have been forced into self-employment and will happily take a paid job if offered one? That would imply there is still plenty of slack in the labour market and monetary policy can stay looser for longer.

But perhaps the structural trend means those paid jobs will not become available. If so, the economy may have created a vast reserve labour force, akin to the “spinsters” of early 19th-century Britain—single women who were paid piece rates for spinning textiles at home—or the dockers who used to mass outside port gates in the hope of being selected for a day's work. That would suggest an economy where wages are permanently kept under pressure and where profit margins remain high. Good news for the stockmarket perhaps, but not so good for the self-employed.

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