

Pension Planning for Entrepreneurs: An actuarial perspective

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The speakers

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Agenda

- Setting the scene
- Who are entrepreneurs/self-employed
- An example market (UK)
- Further analysis
- Considerations:
 - Actuaries and companies
 - Governments and policymakers
- Next steps

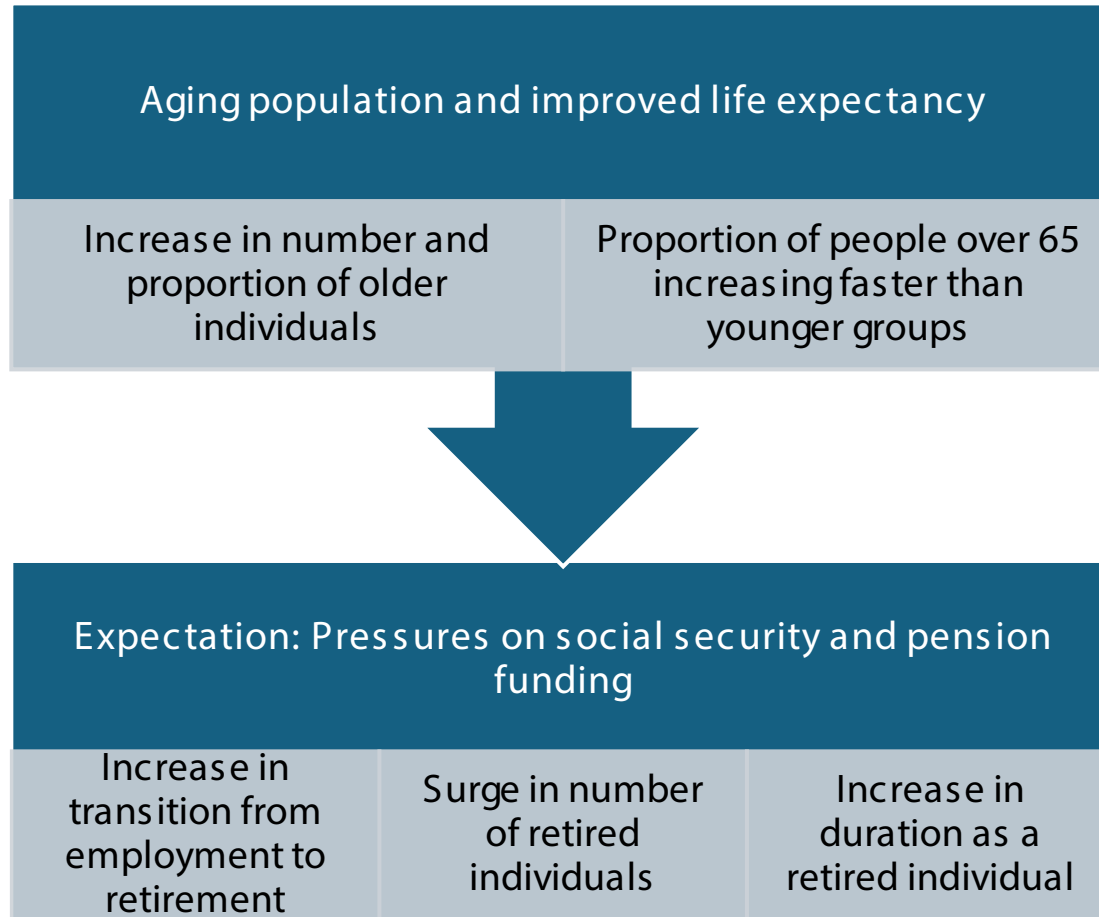
“The global population aged 65 and above is expected to rise from 10% in 2022 to 16% in 2050.

It is projected that by 2050, the number of individuals aged 65 years or above across the world will be twice the number of children under age 5 and almost equivalent to the number of children under 12 years.”

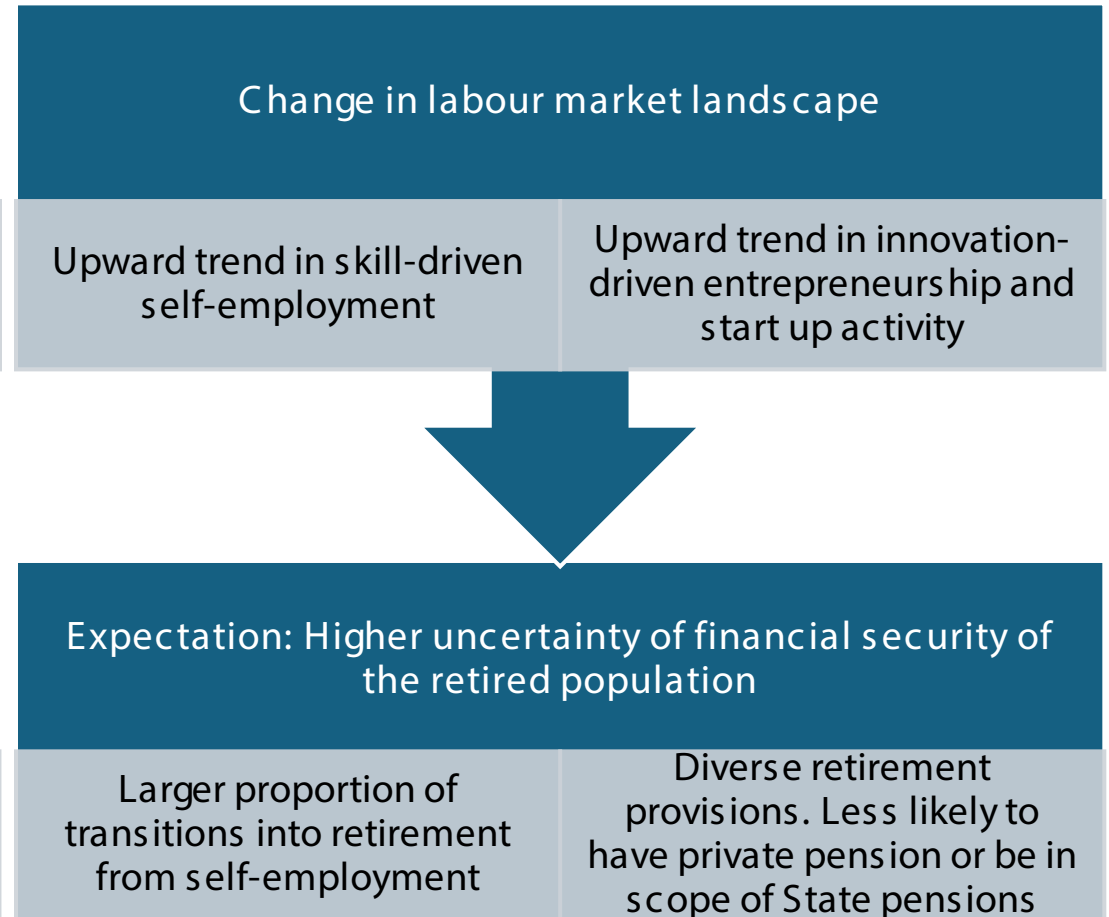
United Nations World Population Prospects 2022

What is the problem?

General problem



Granular problem



Why is it a problem?

Increased likelihood that the self-employed could retire with inadequate private pension provisions and no or insufficient state pension eligibility

Potentially material financial impact on governments as more individuals than expected retire into financial insecurity and remain in a state of financial vulnerability for longer than expected .

Additional pressure on the social security system and risk of increased poverty.

Problem can materialise as early as 10 to 15 years from now.

The pension gap for the self-employed requires evaluation.

Actuaries can influence pre-emptive actions to mitigate its impact.

“Entrepreneurship is the process of creating something new and value by devoting the necessary time and effort, assuming the accompanying financial, psychic, and social risks and receiving the resulting awards of monetary and personal satisfaction and independence”

Hisrich and Peters (1998)

The self-employed are not a homogenous group

Throughout this presentation we use the term self-employed to cover the different types of entrepreneurs.

They can be classified as:

- Skill driven vs innovation driven
- Opportunity based vs necessity based
- Non-standard employment: Dependent and independent self-employed
- Ownership of small/medium enterprises and large businesses

An example market (UK)

We looked at the self-employed and pension provision landscape for the UK, this market was chosen due to:

- Mature and competitive private pension market (i.e. choices)
- Government tax relief on pension contributions (i.e. incentives)
- Existence of initiative to reduce the pension gap (i.e. accessibility)
- Availability of some relevant data.

The UK self-employed: Demographic highlights (2022)

4.1m

Number of self-employed

48

Average age of the self-employed

£278b

Contribution to UK economy

48%

Proportion of the self-employed over 50

13%

Proportion of UK workforce

62%

Males

Notable trends:

- Gender:

Since 2008, the number of women has increased by 57%, while the number of men by 11%. The number of working mothers has increased by 55%.

- Disability:

The numbers of disabled self-employed individuals is increasing year-on-year (42% between 2013 and 2022) with the highest increase being amongst the over 60s.

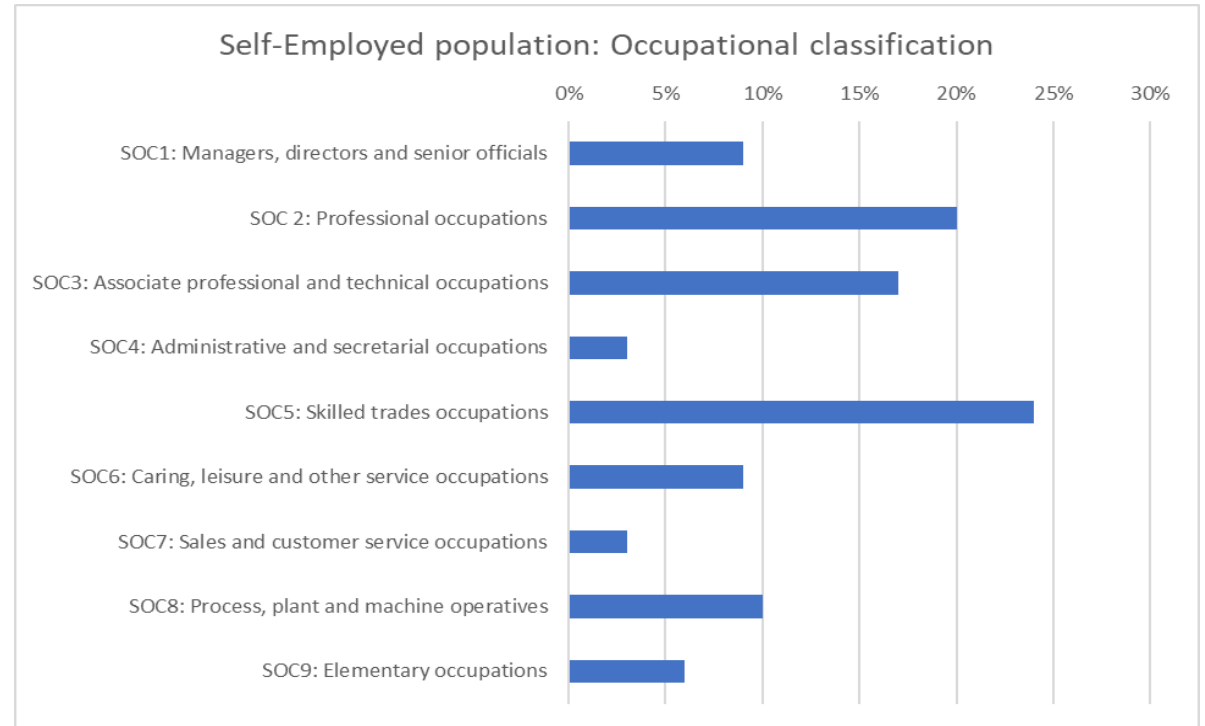
The UK self-employed: Occupational highlights (2022)



There is a wide spectrum of areas in which the self-employed operate.



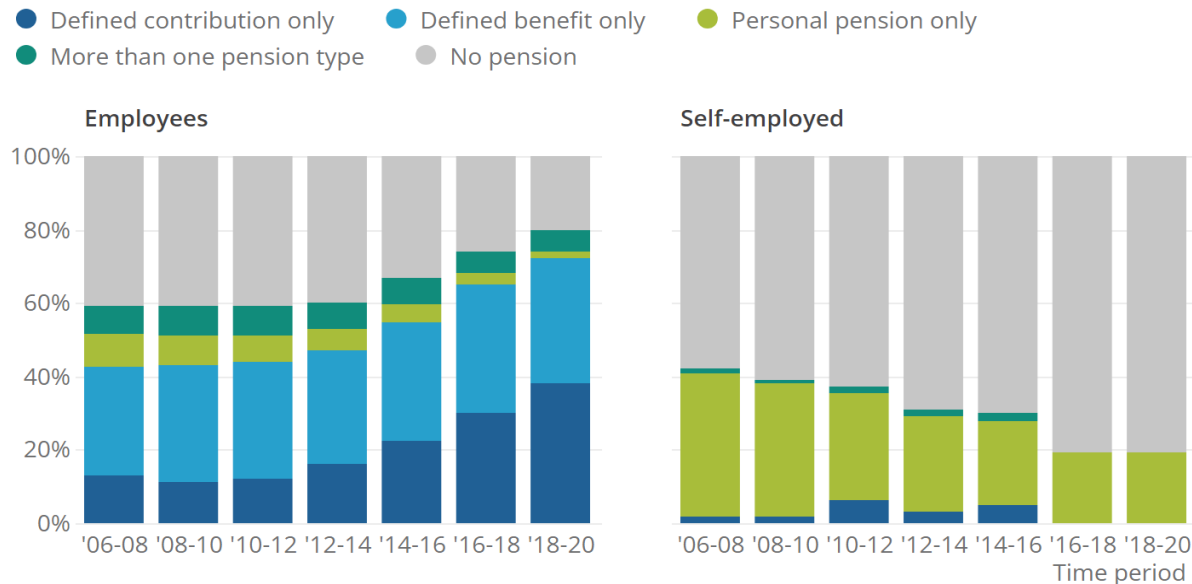
Members of the distinct groups, and indeed within the same group, will have varying levels of financial literacy and a wide range for annual income.



Source: The UK Office for National Statistics (ONS).

SOC: Standard Occupational Classification, used by the ONS and categorises jobs according to the required skill level, qualification and specialisation. 1 represents the highest level of technical skill, qualification and specialisation

The UK self-employed: pension plans held (2006 – 2020)



Source: Saving for retirement in Great Britain: April 2018 to March 2020 - issued by the Office for National Statistics

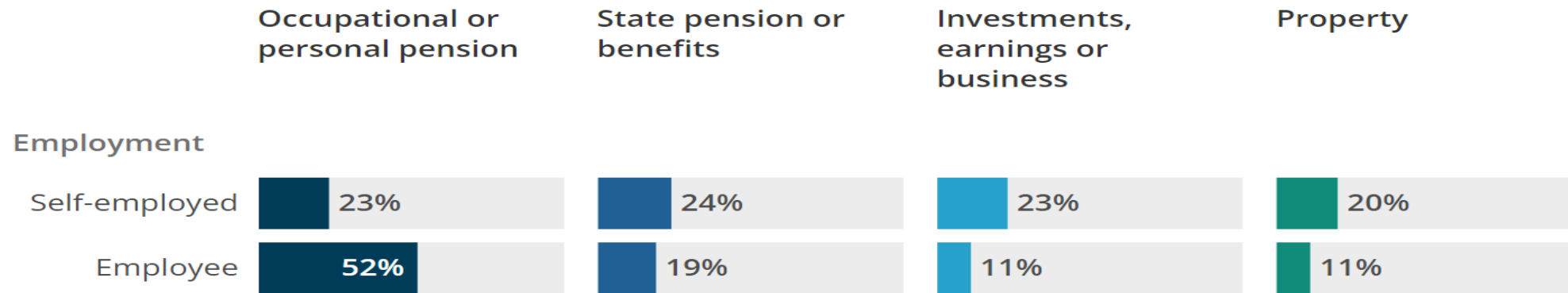
We note that the above graphic summarises data up to the year 2020 only. However, self-employment figures have been relatively stable in the period 2020 to 2022, therefore we do not consider the date difference to be a material limitation to our comparison.

- The self-employed have consistently held less pensions than the employed population.
- The gap is widening over time.
- 20% of the self-employed were saving into a pension (down from c 40% twelve years earlier).

The UK self-employed: Observations

- Pension products are available to the self-employed.
- There are also government actions in terms of the introduction of the National defined contribution scheme, as well as tax incentives when making contributions into a pension or saving plan.
- However, there is still a significant gap in pension coverage for the self-employed.
- The make-up of the self-employed population is changing in terms of gender, age and disability.
- Self-employment is also present in professions at various levels of skill, qualification, and income.
- Yet pension take-up by the self-employed is low
- Narrowing the pension gap for the self-employed has a wide-reaching impact on achieving financial inclusivity and security in society.

The UK self-employed: Sources of income in retirement



Source: Saving for retirement in Great Britain: April 2018 to March 2020 - issued by the Office for National Statistics

- More than twice as much self-employed individuals, compared to the employed, are expecting to finance their retirement from accumulated wealth in property, investments and earning from their business.
- Conversely, more than twice as many employees expect to finance their retirement from occupational or personal pensions, compared to the self-employed
- the self-employed population may have more volatile income in retirement.

Further Analysis and Results

- An explanatory study was conducted to provide some important features to actuaries that can help in closing the gap and allowing for better recognition of the needs in the market.
- LPM models were used to indicate the following relationships:
 - entrepreneurship and pension plans
 - size of business and pension plans

And finally, personal traits and pension plans (a similar study conducted by Balasuriyaa and Yang (2019))

Main findings – pension plans

- Entrepreneurship and pension plans

There is a positive relationship between personal pension and entrepreneurship. This means that Entrepreneurs are likely to get personal pensions.

Whereas a negative association between the employer pension and entrepreneurship is detected indicating that entrepreneurs are less likely to set up an employer pension.

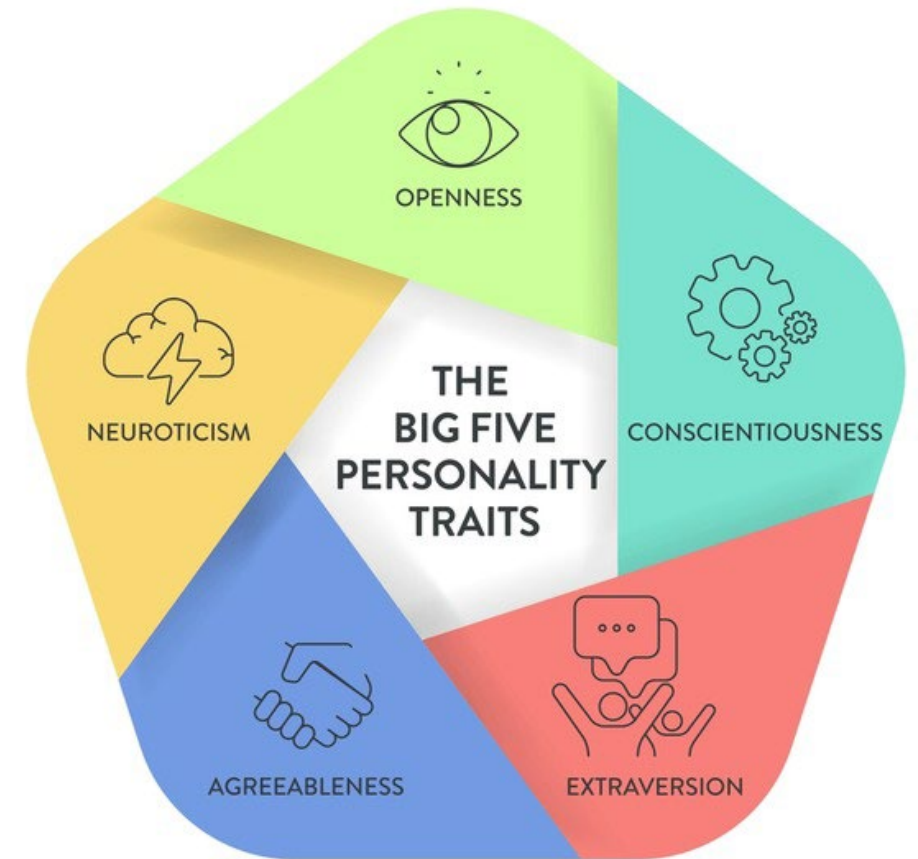
- Size of business and pension plans

The self-employed with employees are more likely to be more prepared with pension plans than the self-employed without employees.

The larger the size of the business the more likely that an employer pension scheme is used.

Main findings – personality traits and pension plans

- The extraverted entrepreneur is more likely to get personal pension.
- In addition, the entrepreneurs who are characterised as conscientious and opened to experience are more likely to get either personal pension or sign up to an employer pension.
- Whilst entrepreneurs with Agreeability and neuroticism traits are less likely to have either personal or employer pensions.



Why may the self-employed avoid private pensions

- Prefer more accessible investments, such as investment accounts and property
- Plan to rely on income streams from their business profits.
- Plan to sell their business and provide retirement income from the sales proceeds
- Individuals may not have trust in pension providers and may perceive pensions to be poor value for money
- There remains a risk that economic conditions or business performance may lead to volatile income streams
- Innovations may lead to the existing business becoming obsolete, leading to no income or sale prospects
- Owning a successful business, whilst indicating business acumen, does not necessarily equate to financial literacy in terms of risk-based thinking for retirement.

Considerations for Actuaries and companies

Product design

- Appeal: Design profitable and flexible products that can be attractive to the self-employed population. E.g. flexibility, accessibility.
- Inform: Clear and transparent awareness campaigns that clarify:
 - The risks of having no pension
 - The risks of having a pension
 - The implications of the uncertainty of future non-pension income

Distribution channels

- Reach: Innovative communication and/or distribution channels may be needed for better reach this includes
 - trade and professional bodies,
 - NGOs and micro-finance entities
 - social media,
 - utilisation of Artificial Intelligence (AI)
 - Tax authorities?
- The personality traits of the self-employed should inform the medium and approach

Commercial

- Risk Profile: Consider the change in the pension providers' risk profile following increased take-up and the impact on business plans
- Equity: Consider equity between offerings for the self-employed and those for the employed population

Considerations for governments and policymakers

- Government financial security objectives should be strongly linked to financial inclusivity.
- Financial literacy initiatives around the uncertainty of cashflows. The risks should be linked to current and expected living standards.
- Financial inclusion and literacy initiatives should consider the availability and affordability of independent financial advice.
- Master trusts (and maybe Superfunds).

Next steps

- A better understanding of the potential magnitude of the self-employed pension gap
 - Actuarial projections and sensitivities that incorporate life expectancy as well as the make-up of the self-employed population and assumptions regarding pension preparedness.
 - This will require collaboration between actuaries and policymakers across the globe
- An accelerated action plan to mitigate the impact of the self-employed retiring in the next 20 years
- Studies of sustainable policies for financial security, inclusion and literacy.
 - Actuarial projections to assess the financial cost of certain proposed policies, strategies and tactics against the general societal benefit.

Comments

Questions