Self-employed predicted a £208,500 pension deficit compared to employed individuals at retirement

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Research from the UK's leading business finance platform, Funding Circle, using HMRC pension statistics, shows the average pension pot for a self-employed worker could sit at just £50,700 at retirement—roughly 15% of that of employees. At current saving rates, this could leave the self-employed facing a retirement income shortfall of £208,500, leaving many reliant on the State Pension alone.

Private Pensions Are Becoming Essential — But the Self-Employed Are Missing Out

As confidence in the State Pension's future wavers, private pensions have never been more important. Employees benefit from automatic enrolment, which ensures regular contributions from both workers and employers. As a result, around 88% of employees are now saving for retirement through workplace pensions.

The picture looks very different for the self-employed. Only one in five currently contributes to a private pension. Rising business costs, irregular income, and ongoing inflation are forcing many to sacrifice their retirement savings just to stay afloat.

The Data Behind the Gap

Self-employed individuals contributed £2.7 billion to private pensions in 2023–24, up from £2.3 billion the previous year. Yet, despite this modest growth, participation remains low. According to the Institute for Fiscal Studies (IFS), 63% of self-employed workers are projected to fall short of their target replacement rate – the level needed to maintain living standards in retirement. The IFS also notes that only around 20% of the self-employed now save into a private pension, and even among those who do, over a quarter make unchanged contributions for five years, meaning their savings are effectively shrinking in real terms.

Meanwhile, 66% are not expected to reach the Pensions and Lifetime Savings Association (PLSA) minimum standard of £13,400 a year (single pensioner, outside London).

Why the Self-Employed Save Less

While 20% of self-employed individuals are reported to be saving into a private pension scheme, there are reasons why they may not be investing in this way.

1. **No Automatic Enrolment**
   Employees are automatically enrolled in workplace pensions, while the self-employed must set one up themselves. This lack of automation requires individuals to seek out which pension provider to choose; with no HR department or employer scheme, choosing and managing a pension can feel daunting.

2. **Irregular Income**
   Variable earnings make it harder to commit to regular pension payments. Often self-employed income can fluctuate month to month or seasonally; this variability can make consistent payments difficult. In tighter months, contributions are often paused or reduced.

3. **Cash Flow Pressures**
   Many self-employed workers prioritise business costs, taxes, and daily expenses over long-term savings. Since the benefits of a pension are years away, the incentive to contribute may feel less urgent.

4. **Alternative Retirement Expectations**
   Some self-employed people believe they can rely on selling a business, property, or other investments instead of a pension. This can reduce motivation to contribute regularly.

5. **Tax Trade-Offs**
   Although pension contributions are tax-deductible, many prefer to reduce taxable profits through immediate business expenses rather than deferred savings.

6. **Psychological Barriers**
   Contributing to a pension is often “invisible” money that you can’t access until retirement. For people managing their own finances daily, this can feel less rewarding than saving in accessible accounts.

The Retirement Deficit

At current saving rates, self-employed workers could retire with £10,000–£11,000 less per year than their target income, even after receiving the full State Pension. Employees, supported by automatic enrolment and employer contributions, are far more likely to meet their retirement goals.

Assume a typical 40-year working life (from age 25 to 65). Employees benefit from automatic enrolment, with around 88% taking part and contributing an average of £3,000 per year. For the self-employed, participation drops to just 20%, with average annual contributions of £2,100.

If we apply a 5% annual investment growth rate over a 40-year career, this results in:

- Employees: a pension pot of roughly £318,000, delivering around £12,720 per year in retirement income.
- Self-employed: a much smaller pot of around £50,700, providing just £2,028 per year.

Adding in the full State Pension (projected at £12,547 per year from 2026) gives:

- Employees: a total annual retirement income of about £25,267
- Self-employed: only £14,575

That’s a £10,425 annual gap, or roughly £208,500 over a 20-year retirement – a significant shortfall that could define the difference between financial comfort and financial strain later in life.

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This widening gap is driven by two key factors:

- **Low participation:** only 20% of the self-employed contribute, versus 88% of employees.
- **Lower contribution levels:** the self-employed typically save £2,100 per year, compared to £3,000 for employees.

Invest in your business's future without sacrificing your own

Funding Circle provides small businesses with:

- Smooth out income fluctuations so they can keep contributing to pensions even when cash flow dips.
- Invest strategically, freeing up personal income for long-term goals like retirement savings.
- Build financial resilience, ensuring that business challenges today don’t undermine financial security tomorrow.

Alexander Allen, Managing Director & Chief Customer Officer at Funding Circle said: "At Funding Circle, we work with thousands of self-employed people and small business owners who face this same balancing act - managing today's cash flow while planning for tomorrow. By improving access to finance, we support small businesses across the UK with a range of products to aid them so they can get on with what they do best, running their business. Our mission has always been to help small businesses grow – but growth shouldn’t stop at your business. It should extend to your personal financial well-being, too."

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