

# Managing in Tough Times

## Rebounding Your Finances after the Great Recession

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*Implementing good money management practices can help you rebound and allow you to be better prepared for future changes in the economy.*

Financial stability is important for most individuals. However, as a result of the recent economic recession, commonly referred to as the Great Recession, many families have found themselves in difficult financial situations. Regardless of age, income level, or education, the majority of Americans were impacted by the recession and the continued slow growth of the economy. In fact, the National Bureau of Economic Research found that between November 2008 and April 2010, four out of 10 American households were unemployed, upside down on their mortgage, or late paying their house payment. Regardless if you have lost your job, a significant portion of your retirement savings, or your home, it is important to realize that you are not alone. Many Americans are striving to manage tough economic times.

### Managing in Tough Times: Taking Control

If your financial situation has changed or the general nature of the economy has placed a strain on your finances, it is important to approach your current financial situation with a plan. Implementing good money management practices can help you rebound and allow you to be better prepared for future changes in the economy.

#### Step One: Identify Your Income

Be realistic with yourself and your spouse about your finances. Start by identifying all monthly income sources. Often individuals think of their paycheck as

their only source of income. However, many people may have other sources of income, such as interest earned on investments, child support payments, unemployment benefits, food stamps, or Social Security. To determine your total income for the month, list each source of income, the amount, and how often you receive the income. For example, if you receive your paycheck twice per month, multiply the amount by two, to determine your monthly income from wages. Do the same for each income source.

#### Step Two: Identify Your Current Expenses

Start by making a list of your *fixed* expenses. Those expenses are usually the same amount and due at the same time each month. Examples of fixed expenses may include your mortgage or rent payment or insurance premiums. Next, identify your *flexible* expenses. Flexible expenses vary from month to month, such as entertainment, food purchased away from home, or personal care items.

If you are struggling to identify your flexible expenses, you may want to keep a spending journal for a week or more to track your spending habits. Have you ever had the experience of having \$50 in your wallet on Monday morning and by Wednesday afternoon, you wonder where that money went? Tracking your flexible expenses will help you answer this question. Write down all of your expenses, including incidentals such as coffee purchased at the gas station. At the end of the week, divide your expenses into different

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categories. Use this as a guide to estimate your flexible expenses for the month. As you track your flexible expenses, you may find ways to scale back or reduce your spending, such as taking your lunch to work instead of eating out.

### **Step Three: Compare Your Income and Expenses**

After you identify your income sources and expenses, compare your total monthly income to your monthly expenses. Use your answers to the following questions as a guide to help you evaluate your current spending habits.

- Are you spending more than you make?
- Are you paying your bills on time?
- Did you include savings as a monthly expense item?

### **Step Four: Scaling Back**

A recent study, found that 40 percent of Americans are living paycheck to paycheck. Often consumers who are “maxed out,” or spend all of their current income, are less likely to be able to adapt to changing economic circumstances, such as price increases on goods and services like gasoline or groceries. However, for many of us scaling back is an option. As you review your expenses answer the following questions:

- Do you have premium television or phone services that you could reduce?
- Do you have subscriptions to magazines or newspapers that you could access for free online?
- Could you take your lunch to work and save on food purchased away from home?
- Do you have any spending leaks, such as dining out, vending machine purchases, late fees, or lottery tickets?

In addition to reducing current expenses, also consider if there are ways you can reduce or delay new expenses or purchases.

Regardless of your current financial situation, tracking your current income and expenses is a sound money management strategy. However, as a result of the recession, your family may have experienced a specific financial crisis or event. If you have experienced a significant change, such as job loss, it is important to develop a recovery plan for your family's finances. A recovery plan includes setting financial

goals and developing a household budget to help your family work toward those goals. Start with the knowledge gained by identifying your income sources and tracking your expenses to develop a spending plan on paper for the next month. Continue to track your expenses and adapt your spending plan as necessary.

### **Managing in Tough Times: Unemployment or Reduction in Hours**

In 2011, almost 12 percent of families had an unemployed member. Unemployment within a family not only creates financial stress, but may also lead to emotional distress. If you or a family member has experienced job loss or you have had a significant reduction in your work hours, you may be eligible to apply for unemployment insurance. Unemployment insurance provides temporary relief to workers, who meet program requirements and were laid off due to no fault of their own. Benefit amounts range from a minimum of \$39 to a maximum of \$415 per week. The amount you receive from unemployment will depend on your previous salary. You can file a claim or learn more about unemployment insurance on the Kentucky Office of Employment and Training website, <http://www.oet.ky.gov/>.

Although your finances may be extremely tight during a period of unemployment, it is important to maintain health insurance. You and your family may be eligible for the Consolidated Omnibus Budget Reconciliation Act (COBRA). COBRA provides you the option of continuing your group health care coverage after you have been separated from an employer. Qualifying events to be eligible for COBRA include a reduction in the number of hours of employment and voluntary or involuntary termination from an employer, unless due to gross misconduct. Furthermore, you must have been enrolled in the employer's health plan prior to the qualifying event resulting in the potential loss of health care benefits. Typically, group health care plans that are maintained by employers with more than 20 employees provide COBRA benefits. Your former employer is not responsible for paying any portion of your insurance premium, but COBRA may be less expensive than seeking your own health insurance plan. Other health insurance options may also be available, depending on your family size and income level. Your children may be eligible for

the Kentucky Children's Health Insurance Program (KCHIP), which is free or low-cost health insurance for children. More information about KCHIP can be found at <http://kidshealth.ky.gov/en/kchip/>.

Finally, you may be tempted to withdraw money from your employer sponsored retirement plan, such as a 401(k) or 403(b). Be cautious of the penalties and taxes associated with taking an early withdrawal from a retirement savings plan before the age of 59½. Early withdrawals can be very costly, including a 10 percent penalty plus ordinary income taxes; therefore, you may want to consider other options for accessing cash before making a withdraw from a tax-deferred retirement account. Additionally, you may want to speak with a tax accountant to learn more about the consequences of early withdrawals. You may want to consider rolling over your retirement savings plan from your employer to another qualified retirement account, such as an Individual Retirement Account or IRA. Transferring your account may provide you with greater investment options.

## Managing in Tough Times: Retiring in Uncertainty

Changing economic conditions have many people reconsidering or delaying retirement. If you had delayed saving for retirement or lost some of your retirement nest egg due to changes in the market, you may wonder if it is still possible to retire.

Generally, there are three strategies that you can use to build your nest egg:

1. Save more money
2. Invest better
3. Retire later than you originally planned

### Step One: Identify your Retirement Goals

Identifying your retirement goals will help you determine how much money or income you will need to meet the retirement lifestyle that you have in mind.

### Step Two: Compare Your Anticipated Retirement Income and Expenses

Make a list of all your retirement income sources; include income from Social Security, 401(k) and 403(b), IRAs, and other investments. Next, review your list of current expenses, and individually evaluate each category. Do you anticipate it increasing, decreasing, or staying the same? Typically, retirees need 70 to 80 percent of their current income to cover their retirement expenses. This will vary based on your

situation. Once you have estimated your retirement income and expenses, you will be able to determine how close you are to reaching your goal.

### Step Three: Automate Your Retirement Savings

Consider automating your retirement savings. Deducting a portion of your paycheck to go directly into a retirement savings or investment account is an easy way to build your savings. Automating your savings takes less time on your part and will be consistent every month. You may also consider adding extra hours at work or picking up a second job. Extra income should be applied directly to your retirement investment accounts.

### Step Four: Make Wise Investment Choices

As you build your retirement savings, it is important to make wise investment choices. Many employers will often match a portion of employee contributions. If this is the case, be certain to maximize your contribution to this account first, up to the amount your employer will match. The employer match is essentially "free money," that you do not receive if you are not participating in the retirement plan. Furthermore, your contribution can be deducted from your paycheck before taxes are withheld; thus lowering your taxable income.

Other types of retirement investments may include IRAs, stocks, fixed-income investments, mutual funds, and cash savings. Prior to selecting your retirement investments, be certain to do your research; you may also consider meeting with a Certified Financial Planner. Look at the long-term performance of investments and assess the level of risk. Remember high risk investments will typically yield the greatest awards or the biggest losses. For individuals approaching retirement age, maintain more conservative investments, since you are anticipating needing the money in the near future. Be certain to diversify your investments. Placing your retirement savings into several different types of investments may help reduce your risk. Do not try to guess the market, consistent investing over a period of time will most likely yield a greater return than trying to guess when to buy or sell based on fluctuations in the market.

### Step Five: Consider Working Longer

Some individuals may need to consider working longer to meet their retirement income needs. You may choose to work longer at your current profession or retire and then seek a part-time retirement job.

With your retirement income from your previous employer, such as a 401(k) or 403(b), in addition to your other retirement investments, you may find that you are able to work part-time, for lower wages, and still have adequate income during retirement.

## Managing in Tough Times: Struggling with Your Mortgage

As a result of the recession, home values significantly declined. At the end of 2011, more than 25 percent of homeowners with a mortgage were at or near-negative equity, meaning they owed more on their home than it was worth. The numbers of homes in foreclosure have increased significantly in recent years. However, just because you have little or no equity in your home does not necessarily mean you are in danger of foreclosure or even in financial crisis. It may indicate a cause for concern if you need to sell your home or refinance. Yet, if you are struggling to make or are behind on your mortgage payments, contact your mortgage lender to discuss your options. If you have only missed a few payments or if your problem is a result of a temporary situation, you may be able to negotiate a repayment plan or a temporary forbearance with your mortgage lender. If the problem is not temporary, you may consider discussing a loan modification with your lender. A loan modification

can include a change in terms, such as interest rate or repayment period, to allow your loan to be more affordable. Finally, you may need to consider selling your home. Any change in loan terms or the solution established with your lender needs to be in writing.

Often financial difficulties can feel overwhelming. However, developing and implementing a plan specific for the financial event that you or your family is experiencing is the first step in overcoming a financial crisis.

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