SURVIVING A RECESSION

How to Weather an Economic Downturn

Surviving a Recession

How to Weather an Economic Downturn

Recessions are a fact of life. Our economy can't keep growing forever, so it's only natural for there to be downturns. Every boom has an eventual bust. That's what a recession is. It's a period where economic activity slows down significantly, affecting both businesses and consumers.

When we have **two or more consecutive quarters of economic decline**, it's a recession. According to U.S. economic history, this happens about **every four years**, although it's not always exact. Still, whether the next recession is on time or not, it will eventually come, so it's important that you prepare your finances for it.

What's at stake during a recession?

You might think that if you're not an investor, an economic downturn doesn't affect you. But a recession is more than just headlines about stock market crashes. And even those crashes can affect you if you're saving for retirement.

Here are all the ways that a recession can affect average Americans:

- **Unemployment.** A recession often coincides with a spike in unemployment. As business slows, companies are more likely to have layoffs. You need to be prepared for the possibility that you could lose your job.
- **Pay cuts, reduced hours.** Even companies that don't lay off employees may have pay cuts or reduced hours. It was common during the Great Recession as well as the pandemic recession for businesses to go down to a 4-day workweek. Hourly-waged employees effectively lose 20%

of their income when this happens.

- **Less opportunity for career advancement.** Many companies will also stop providing annual reviews and salary increases during a recession. It can also be harder to find new employment with a good salary. There's also higher competition for available jobs, given that unemployment is higher.
- **Lower savings rates.** When the economy slows, the Federal Reserve cuts interest rates to encourage banks to lend money and consumers to borrow. However, this also means that interest rates on savings accounts get cut, too. This can have a bigger impact if you have money saved in a high-growth variable-rate account, such as a Money Market Account (MMA).
- **Retirement investments.** If you're saving for retirement through a 401(k) or IRA then changes in the stock market can affect your savings significantly. Workers that are nearing retirement when a recession strikes need to be especially concerned because your investments may not have time to recover, which could delay your retirement.

- **Cut credit limits.** Credit card companies may cut credit limits during a recession, sometimes without notice. They will decrease limits to avoid consumers running up big balances that they won't be able to pay back. This can hurt your credit score because a lower credit limit can increase how much of your available limit you're using. That's the second biggest factor used to calculate your credit score.

- **Stricter lending standards.** Buying a car or a home or getting a personal loan to consolidate debt can all be harder during a recession. Even though interest rates are low, which is beneficial, lenders may increase credit score and debt-to-income ratio requirements. So, it can be tough to get approved to take advantage of those low rates.
- **Negative equity.** In extreme cases, such as the Great Recession which included a housing market crash, millions of homeowners were "upside-down" on their mortgages. Home values fell and people who had recently purchased their homes or had borrowed against their equity found that they owed more than their home was worth. People who sold homes during this time dealt with short sales, where they took a loss on the sale and didn't have funds to put a down payment on a new home.
- **Higher risk of delinquencies, defaults, repossession, and foreclosure.** Delinquency rates typically rise during a recession because people struggle to pay their bills. If you can't catch up, you could face repossession of your car or foreclosure on your home. Even if you can't pay your credit cards, this can quickly decrease your credit score, making it harder to recover and rebuild.

We're in a recession. What now?

Ideally, you're reading this guide before a recession hits, so you can be prepared. If so, you can skip forward to **"Preparing for the Next Recession."**

But more than likely, you're reading this guide because we're in a recession now and you're worried about your finances or already struggling. In this case, follow these steps:

Step 1: Review your budget and cut as much as possible

Even if you're not already dealing with income loss, this step is essential. You need more money to pay off debt and save aggressively. So, it's time to create an emergency budget. If it isn't a necessity, it needs to go.

- Review all your expenses to see what you don't need – nice-to-haves like your daily trip to the barista or spending money in entertainment apps should be the first things to go
- If you have things like duplicate streaming services, cut back to one
- Limit subscription services, whether it's magazine and newspaper subscriptions or box delivery subscription services
- If there are services you can do yourself, like landscaping, house cleaning, or pool maintenance, cut the paid service and divide the new chores amongst members of your household
- Evaluate how much you spend on necessities, like groceries, to see if there are ways to cut back

Keep in mind that these cuts are temporary. You're doing this to weather a storm. Once the storm is over, you can add those luxuries that you cut back in. But you need to do everything possible to protect your finances now.

If you don't already have a formal budget in place, it's time to make one. The “Budgeting Made Easy” guide in this same publication series can help you get started.

Step 2: Assess your savings and assets

Next, you need to evaluate your savings and assets to see how big of a financial safety net you have.

First, check your savings. Ideally, in normal circumstances, you should have enough in savings to cover 3-6 months of bills and budgeted expenses. This will provide some breathing room in case you lose your job during the downturn.

Also, look at any cash equivalent assets you have. These are any assets that can quickly be converted to cash, such as:

- Money Market Accounts (MMAs)
- Certificates of Deposit (CDs)
- Treasury Bills (T-Bills)
- Short-term Government Bonds

Evaluate all these cash equivalents to see how much additional money you could generate if needed.

Step 3: Look for additional sources of income

This step is essential for those who are unemployed or have lost income. As you look for full-time employment in your chosen career field, you need to find ways to keep up with your bills as much as possible.

Even if you are still employed and receiving your full salary, it's a good idea to assess new income opportunities. You want to look for outlets that can increase your income, so you have more money to save and pay off any debt you may have.

These questions can help you get started:

- Do you have items in your home that you can sell for cash?
- Can you pick up small jobs on the side through consulting or freelance work?
- Do you have time to pick up a side gig, such as food delivery, ridesharing, or childcare to supplement your income?
- If you're still employed and receive hourly wages, can you pick up extra shifts or work overtime with your manager's approval?

Maximizing your income during a recession is critical. If you lost your job, a side job or temporary work may not fully replace your income, but it can help you stay afloat as much as possible. Everything you can pay now means once less bill that you will need to catch up on later.

Step 4: Educate yourself on resources that may be available to you

Regardless of your situation, it's a good idea to take time to understand the benefits and relief resources that may be available to you.

Unemployment benefits should be available to workers who are laid off during a recession. You receive these benefits through your state's unemployment insurance office, which you can find through careeronestop.org.

Also familiarize yourself with federal, state, and local resources that may be available for housing, utilities, healthcare, food insecurity, and work. You can learn about local resources through the 211 service in your local area. Simply call 211 or visit 211.org.

If you are still employed, check into any severance packages that you may be entitled to. Also, review your company's policy on providing compensation for unused PTO. Knowing how much money you may receive if you get laid off can give you a head start maintaining stability if you lose your job.

Step 5: If you have the means, focus on paying off debt

During a recession, your primary focus needs to be on keeping up with rent or mortgage payments and essential bills. The next priority should be on paying off debt.

High-interest rate credit card debt, in particular, is not good to carry during a recession. Accrued monthly interest charges eat away at the income that you could use to build your savings. And each debt you pay off is one less bill you need to worry about.

If you have multiple credit card balances, consider consolidating them with a balance transfer credit card or personal loan. This can help lower the interest rate applied to the balance so you can pay it off faster.

If you don't have good enough credit to qualify for those options, contact a credit counseling agency. You may be able to enroll in a debt management program, which can reduce your total credit card payments by up to 50%.

Step 6: Maximize your savings

In addition to having your debt under control, focus on building your savings. In a recession, it's a good idea to increase the size of your emergency fund. Instead of having 3-6 months of bills and necessary expenses saved, aim for 6-12 months.

This increased financial cushion will help protect you in case the recession drags on and leads to prolonged periods of unemployment and pay cuts.

What to do if you're already falling behind

These tips can help you minimize financial issues during a period of hardship:

- **If you haven't done so already, apply for unemployment immediately.** Check state guidelines on who qualifies for unemployment and what steps you need to take to receive benefits. Some states have very specific rules you will need to follow.
- **Call your mortgage lender or landlord at the first sign of trouble making your payments.** Let them know about your situation and see if they would defer your payments for a time.
    - Deferment temporarily pauses or reduces your payments until you can get back on your feet.
    - Remember, that your mortgage and rent should be paid first before any other bills. You don't want to face eviction or foreclosure during a recession.
- **Apply for deferment or forbearance on federal student loans.** Deferment will temporarily suspend your payments; if you have subsidized loans, interest will not accrue, but

it will on unsubsidized loans. If you do not qualify for deferment, forbearance can reduce your payments.

- **Contact your other creditors and lenders.** Explain your situation and see if they are willing to suspend or reduce your payments for a time.
  - Keep in mind that creditors are often willing to work with people if they are proactive and contact them as soon as possible—especially in a recession.
  - Hiding from creditors is not recommended. If they cannot reach you, then you are more likely to face added fees, penalty interest, and collection accounts quickly.
- **Keep track of where bills stand** so you're on top of what has been deferred, what payments you need to make, and what's falling behind.
  - Keeping a detailed log of where your credit cards and loans stand will make it easier to catch up once your income has recovered.
- **Avoid using credit to cover cash shortfalls—especially short-term installment loans and payday loans.** Taking on debt to get by during a period of hardship puts you farther behind.
  - Payday loans and high-interest short-term installment loans have extremely high-interest rates and unfavorable terms if you can't pay the debt off quickly. If you are already facing hardship, they are only going to make a bad situation worse.
- **Stay updated on government relief programs that may be available.** Check national news for federal relief efforts; follow a local news source for state, county, and municipal

help. Sign up for your city or county's newsletter or social networks for the latest information on local help.

Steps to take once your income recovers

1. Set a new budget based on your new income to make sure you will spend less than you earn.
    a. Avoid adding discretionary expenses (wants) back in until you have your finances fully under control.
    b. Make sure to allocate money (ideally 5-10%) for rebuilding your emergency savings.
    c. Dedicate all extra cash to paying off your debts and catching up on bills.
2. Prioritize debts for repayment using your credit card debt and borrowing worksheets to help you.
    a. Catch up on secured debts (mortgage, auto loan) first if they are behind.
    b. Focus on debts that are behind but not charged off or defaulted first to keep the accounts open.
    c. Federal student loans can be brought current by making nine out of ten months of payments.
3. Collections should be paid last and fully verified before you agree to any payments.
    a. Check the statute of limitations on collections in your state to ensure the collector can pursue you in court for the debt.
    b. Verify the debt with a debt validation letter from the collector. They must have complete information about you, the debt, and who owns the debt.
    c. Read "Protect Yourself from Debt Collectors" from

this publication series for more tips on how to deal with collection accounts.

4. If you are overwhelmed by the amount of debt that you have, contact a nonprofit credit counseling organization to discuss options for getting out of debt.

Preparing for the next recession

If you are worried that a recession is on its way, there are some practical steps that you can take to prepare:

- **Increase the size of your emergency savings fund.** Ideally, you want 6-12 months of budgeted expenses saved in an easily assessable account.
- **Pay off all outstanding credit card debt.** The fewer bills and obligations, the better. This will also maximize your credit score in case you need to refinance or apply for new credit.
- **Avoid borrowing against the equity in your home.** Adding a second mortgage with a home equity loan or HELOC before a recession can be risky, so avoid it if possible.
- **Consult with your retirement plan advisor to see if you need to adjust your strategy.** All retirement plan advisors offer a free annual evaluation that you can use to your advantage. If you don't have your 401(k) plan advisor's contact information, ask HR for it.
- **Review your budget to see if you have any expenses that you can cut or cut back.** You want to eliminate overspending and stick to your budget strictly.
- **Check your credit.** You can take advantage of your free

annual credit report through annualcreditreport.com. Make sure your credit is clean and error-free, in case you need to borrow or refinance.

- **Review any employment contracts.** Check for severance packages and pay for unused PTO policies.
- **Update your resume and online professional profiles.** If you were to lose your job, you need to be prepared to start a job search immediately. If you have a website or portfolio, make sure the information is up-to-date.