

## Surviving Tough Economic Times

Mary Rowland Personal Finance Column – November 2008

The entire U.S. financial system seems to be collapsing around us this summer and fall. Now, while scary financial doings are on our minds, this is a good time to clean up our own balance sheets and reduce exposure to debt.

The current debacle began with the risky loans in the sub-prime mortgage market. It turned out that these mortgages were everywhere—in bond funds and money market accounts and nearly everything else.

When the loans began to go bad, one bank failure came on the heels of another. Then the Federal Reserve Bank of New York engineered the demise of the failing investment bank, Bear Stearns. Before long the federal government seized control of the two mortgage giants, Fannie Mae and Freddie Mac. Next, the investment bank of Lehman Brothers filed for bankruptcy. And Merrill Lynch was forced to sell itself to Bank of America in a fire sale.

Alan Greenspan, former chairman of the Federal Reserve Bank, said the U.S. was mired in a “once-in-a century” financial crisis that was likely to spark a recession. He added that the crisis was the worst he’s seen in his career and that it still has a long way to go.

So where’s the silver lining? The huge restructuring that will occur in the financial industry over the next several years. Change always means opportunity. To get ready for opportunity, we need to hunker down, get out of debt and become independent.

**IF YOU ARE JUST STARTING** out in your career, and your job is secure, congratulations! Now do your best to pay down debt. Paying off school loans and credit card debt produces a guaranteed return. Your money will earn whatever you are now paying in interest.

For example, if you are carrying a balance of \$1,000 at 18 percent interest, paying it off will give you a return of 18 percent. There is no other guaranteed investment that will provide anything close to that in return.

The most efficient way to pay off debt is to figure out how much extra you can pay per month on your debt. Then put all the extra dollars on the account with the highest interest rate. Pay only the minimum on the others. Continue until you’ve paid off the highest rate card and then do the same thing with the next highest rate card. Be sure to pay the minimum on all the others.

The financial markets and housing markets are in chaos. You should aim to be debt free and ready to move when the turmoil clears up.

**IF YOU ARE AT MID-CAREER**, you might be excused for feeling that everything in your life is collapsing at once: The stock market, the housing market and the availability of student loans. Many students were forced to delay their college careers this fall due to the lack of loans that had been promised. But if you have a secure job, that is something major to be thankful for.

Of course you can’t fight on all fronts. But you, too, should pay off short-term debt. If you have a child going to college soon, begin collecting all the information you will need to apply for financial aid and start planning.

Do not sell stocks. The market has been trading so low that an argument could be made for buying selectively. But be certain your savings and investments are well diversified. Use mutual funds. Bonds are a conservative

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investment, but only if you use them conservatively. Do not buy into any of the get-rich-quick schemes that always arise during troubled markets when people feel desperate about losing money and want to do something to get it back quickly.

IF YOU ARE ABOUT TO RETIRE or are already retired, don't panic. This is a scary economic time but it will pass. You, too, should pay off debt. Pay off all credit cards and consumer loans if you can. Then pay down your mortgage, as it will give you more flexibility in retirement.

Retirees should have diversified investments. Don't sell your stocks now. This is the worst time to sell. And you don't want to be completely out of the stock market in retirement because you need stocks for growth over the long term. But invest wisely, in a diversified and conservative mutual fund with low fees.

You should also have money in bonds. But with the mortgage and credit crisis of the past two years, be especially careful in picking bonds. Don't buy bonds by shopping for the highest yield. The highest yielding bonds are junk. Junk means that the bond must pay more to attract investors because the bonds are much riskier.

Buy only Treasury bonds or corporate bonds with an AAA rating. Be suspicious of any bond investment that claims to be "high-yield," "superior yield" or "enhanced yield." These are other names for junk. In fact, be suspicious of any investment that pays far more than others in its category. Offering super-high interest rates can mean that the company is desperate for cash.

This is a particularly good time to think about the cyclical nature of the financial markets. When prices are soaring—on stocks or homes or whatever—good sense says you take a back seat and wait. We're now in the bust-up phase. Get ready to start up again.

*Mary Rowland is a nationally known business and finance writer. The former personal finance columnist for The New York Times and former co-host of a nationally syndicated radio show, Ms. Rowland is the author of several investment books and speaks regularly to consumers and financial planners about investing and personal finance.*