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Counselors say budgeting can limit pain of layoffs

By CHRIS BAGLEY - Staff Writer

The ideal time for saving money for emergencies may have passed, given that a half-million Californians have lost their jobs to the recession.

But the lightning pace of layoffs and pay cuts since summer underscore the need to prepare for financial hardships months and even years in advance, financial advisers say. And continuing job losses mean that saving and spending wisely are as important as ever.

Rick Mayes, a financial planner in Carlsbad, advises workers to put at least 10 percent of their wages into a rainy-day fund. That's for emergencies ranging from a job loss to a broken washing machine to unexpected medical expenses. It doesn't include what they might be saving for a new car, a house, or other purchases, nor the 10 percent to 15 percent he said they should save for retirement.

A frequently cited rule of thumb is that a rainy-day fund should be large enough to cover three months of expenses. Candace Bahr, another adviser in Carlsbad, said the severity of the recession should probably get people thinking about saving up enough in the future to go for six or 12 months without work.

Home-equity lines of credit can be tapped when the savings begin to run low, Bahr said. The interest rate on a home-equity loan is usually vastly lower than those on revolving credit card balances, which advisers say should be used as a last resort.

But it's better to save money ahead of time than it is to borrow, Bahr said. And the housing bubble's implosion has left many homeowners with little or no equity, she noted: Median home prices have fallen by 44 percent in San Diego County and by 56 percent in Riverside County, according to MDA DataQuick.

Applying early is important because it's tough to qualify for a home equity loan after being laid off, she said.

In the case of a sudden and surprising layoff, Mayes advises taking three days to regroup mentally and emotionally. Otherwise, it can be tough to make sound decisions about what to do next, he said.

Necessary vs. nice

The next step is to list expenses for the last month and sort out the "nice-to-have" items from the necessary ---- and from the absolutely necessary, Mayes said. He suggests paying particular attention to recurring expenses: If a \$70 cable television or cell phone bill doesn't seem large in March, it will definitely seem that way in November after eight months of unemployment, he said.

Depending on a family's savings, cutting that sort of recurring discretionary expense should be one of the first moves, Mayes said. Personal-care expenses such as cologne and beauty supplies are other candidates for early cuts, he said. It's also wise to consider replacing expensive or gas-guzzling vehicles with a reliable and less expensive car, he said.

Mortgage payments above a required minimum also deserve a second look, Mayes said. Homeowners should usually continue to pay down principal, but a laid-off person should probably delay an effort to pay off the mortgage ahead of time. The same logic applies to variable life-insurance policies whose future premiums can be reduced if the insured person overpays by smaller amounts beforehand.

Bahr said all expenses should be on the table.

"Cut back as far as you can as deep as you possibly can," she said.

On average, Americans are already doing that more dramatically than at any point since the Great Depression, according to federal data. Americans' savings rate fell steeply from the early 1990s into the summer of 2008. Economists say the thinner cushions of savings have created a situation where laid-off people have to cut their spending (Feb. 25, 2009) more sharply than ever before, triggering new rounds of layoffs. Anecdotal evidence suggests that workers worried about losing their jobs also curtail spending, albeit less dramatically.

Rule No. 1

Bahr said that domino effect doesn't change the advice she gives to clients.

"The No. 1 rule is that you have to take care of your family first," she said.

Bahr and Mayes alike advise laid-off people to apply for unemployment benefits immediately.

Health insurance is another important matter to consider, they said. Portions of 1986 federal law commonly known as the Consolidated Omnibus Budget Reconciliation Act have required insurers to keep laid-off workers on their plans for 18 months, provided that the insured pay the full monthly cost plus a 2 percent administration fee ---- 102 percent of the premiums.

Recent federal legislation temporarily subsidizes those premiums, reducing workers' obligation to 35 percent.

Terminated employees should cover themselves and their families under individual policies in cases where COBRA coverage still doesn't pencil out, Mayes said. Policies with high deductibles can guard against catastrophic losses while carrying relatively low monthly payments.

"Don't go naked without any health insurance," Mayes said. "That'd be a very bad idea."

Contact staff writer Chris Bagley at (760) 740-5444 or cbagley@nctimes.com. Bagley blogs about local economic trends at <http://bizblogs.nctimes.com>.