

Essential Personal Finance Skills for the “New Normal”: 10 Things That Consumers Need to Know

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Three Topics in 15 Minutes

- “New Normal” realities
- 10 essential personal finance skills
- Rutgers University research: Differences in pre- and post-financial crisis financial practices



We didn't just have a perfect storm...

...We had a perfect **TORNADO!!!**



The "Paradox of Thrift" (Economics Term)

What's good for individuals (e.g., saving more, spending less) is bad for the economy when everyone does it.

Keeping Up With the Smiths | The fallout from one family's belt tightening

The infographic consists of four vertical columns of 3D blocks, each representing a different business affected by the Smiths' spending cuts. The columns are colored green, blue, yellow, and red from left to right. Each column has a small icon at the top: a shopping bag for the green column, a fork and knife for the blue column, a coffee cup for the yellow column, and a mobile phone for the red column.

- Green Column:** The Smiths stop shopping at Brighton Collectibles...
Causing job worries for store manager Carol Rice...
Who eats out less at BJ's Brewhouse.
- Blue Column:** The Smiths also stop eating out...
As Applebee's revenues fall...
and its parent company, DineEquity lays off workers.
- Yellow Column:** The Smiths stop getting lattes...
As Starbucks closes 28 stores in the Dallas area.
- Red Column:** The Smiths cut back on phone service...
As AT&T lays off 12,000 workers.

A12 *Thursday, January 29, 2009*

Many families in the Dallas area, including the Smiths, above, had to cut back on spending, hurting local businesses.

Recent Financial Shocks



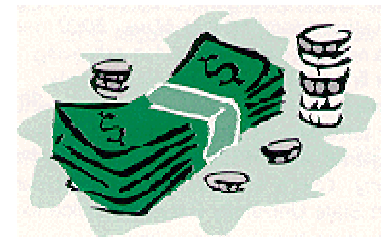
- Recession/Shrinking economy (GDP)
- Collapsed and merged investment banks
- Bank failures and government takeovers

- Mortgage defaults and high foreclosure rates
- Declining home values
- High unemployment rates
- Bear market/stock market volatility
- Increased poverty rates and rich-poor “wealth gaps”
- “The Paradox of Thrift”



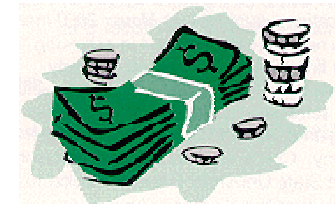
Four Common Aftermaths of Financial Crises

- Deep and prolonged asset market collapses
 - Housing prices
 - Stock market indices
- Profound declines in output (deleveraging)
- High unemployment (in both public and private sector)
- Explosion in government debt as tax revenues decline



Baby Boomers and Older Gen Xers Especially Affected By the Financial Crisis

- Fully experienced, not just one asset bubble- BUT TWO- during long stretches of their working lives
 - “Tech Bubble” and extraordinary run of double-digit stock market returns in late 1990s
 - “Housing Bubble” during much of the 2000s
- Limited recovery time for battered investments
- *Money Magazine* (April 2009):



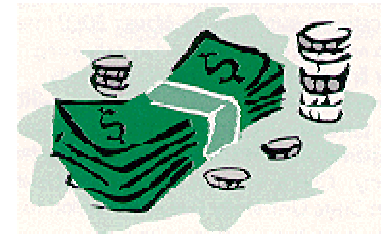
“A generation of Americans grew into middle age thinking that they had more wealth than they really did and their future was a lot more secure than it really was.”

Characteristics of the “New Normal”

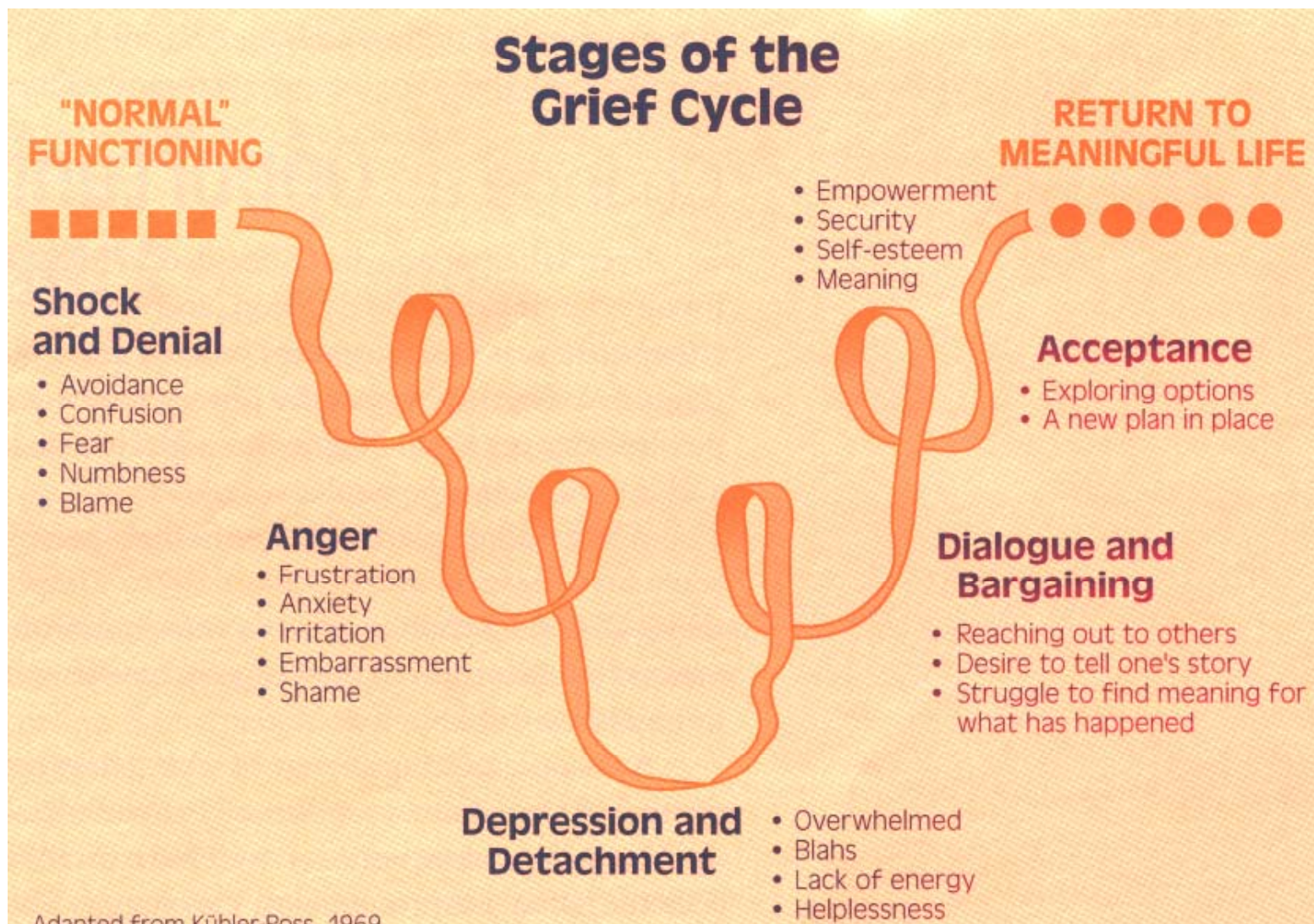
An extended period of:

- Slow U.S. economic growth
- Low single-digit average annual stock returns
- Stubbornly high unemployment levels
- Precarious job security (public and private sector)
- Tightened credit standards for loans
- Increased household savings and debt repayment
- Decreased household spending

- Ultimately, when financial crisis abates, higher inflation (?)
(**minority view**: deleveraging will negate government debt)



Five Stages: How People Receive “Bad News” (Elizabeth Kubler-Ross Model)



Financial Educators and Advisors Can Help Consumers Define Their “New Normal”

- Acknowledge (grieve) “what was,” but don’t dwell on it
- Focus on acceptance, action, and progress
- Build “financial capability” (i.e., what people do with knowledge about money)
- Develop or reassess financial goals
- Reassess post-financial crisis investment risk tolerance



10 Key Financial Learning Needs

1. "The Basics" (e.g., expense tracking, emergency funds, goals)
2. Living on a reduced income (e.g., "stepping down," substitutions)
3. Entrepreneurship skills (increased self-employment is predicted)
4. Budgeting for variable incomes ("cash flow calendar")
5. Estimated tax withholding for "freelance nation" workers
6. Self-funded retirement plans and health insurance
7. Options for "underwater" homeowners
8. Investment characteristics and techniques
9. "Catch-up" retirement planning strategies
10. Human capital investments (including health); increases resilience



Rutgers Research Study: Are Post-Financial Crisis Financial Practices Any Different?

- Data collected from online Financial Fitness Quiz
- URL: <http://njaes.rutgers.edu/money/ffquiz/>
- Quiz includes 20 recommended financial practices
- Total quiz scores can range from 20 to 100
- “Time stamp” tells when data were collected
- N = 6,700 respondents (1/1/07 – 6/30/10)- 42 months
 - 3,212 from 1/1/07 - 11/30/08
 - 3,488 from 12/1/08 – 6/30/10)
 - Self-reported financial practices
- Chose 12/1/08 as cut-off: financial crisis was widely acknowledged; unemployment concerns



Eight Financial Practices Showed Significant-But Very Modest- Time Period Differences

Increased Frequency of Performance (5)

- Written financial goals with a date and cost
- Written spending plan (budget)
- Adequate insurance for big expenses
- Pay credit card bills in full to avoid interest
- Avoid impulse buying & recreational shopping

Decreased Frequency of Performance (3)

- Personal investment account for retirement other than employer pension
- Money spread across more than one type of investment
- Average after-tax yield on savings and investments greater than inflation rate



Don't Get Too Comfortable, Though: Things Will Eventually Change....Again

