



Surviving a Recession? Yes, You Can!

This week, our focus is on a topic facing people the world over, that is, the fear of a recession. Almost daily, we hear about the global financial crisis which has plunged many companies into bankruptcy. The financial problems faced by these companies are as a result of the effects of a recession. Surprisingly, however, their collapse only exacerbates the effects of the recession. This week we will try to define a recession, how the economy and market behave during a recession and what we can do to prepare and ride out a recession.

What is a recession?

A recession has been defined as a period of economic retraction i.e. where the economy actually gets smaller. A couple of the signs that a country is going through a recession are two months of a decline in the GDP (Gross Domestic Product) or a sharp rise in unemployment.

How does the market behave during a recession?

During a recession, household spending usually decreases as a result of possible retrenchment and increases in savings. The decreases in spending affects companies' bottom line as their income levels would decline thus affecting their profitability. This would inadvertently affect share prices as stock prices are directly affected by profitability.

With decreased profitability, companies decrease their inventory and reorder levels. Manufacturers would now have to cut back on production because of the decrease in demand. Inevitably, because of the decrease in demand, companies would be forced to cut back on their staff. Because of the discrepancy between the number of people looking for work and the jobs available, wage levels may decrease.

How Do You Prepare For a Recession?

There are three keys points in preparing for a recession:

- **Awareness:** this involves knowing the causes and consequences of the recessions and how it may affect you.
- **Planning:** preparing a strategy is key to surviving a recession. You must revisit your spending habits and avoid unnecessary spending.

- **Investment:** although most people may think that this is a bad time to invest, this is not always the case. Stock prices are usually low during recessions and some investors choose this time to buy.

Things to keep in mind in your recession planning:

- Create an emergency fund equal to about six months of living expenses. This is to ensure that in case you are terminated you can survive reasonably well.
- Keep these funds liquid i.e. in a savings account as you may need to access them on short notice.
- Revisit your goals. Because of the change in the economy, you may now have to cut back on spending and probably defer plans to sometime in the future.
- Examine your risk tolerance. For some people this may not be possible so we suggest your financial planner do this for you. Your risk tolerance would change during a recession so it is important that you examine this.
- Review and adjust your portfolio accordingly. If there is a possibility that you may lose your job, you should ensure that most, if not all, your investments have very low risk so that the probability of you losing your investment would be minimized.

Budget and Save...Now!

Recessions are usually times of slowdown and low productivity. It is however, important to note that this is usually a stage in the natural business cycle. Most, if not all, countries and businesses come out of recessions. Therefore, we can see this period as preparation for a rebirth of business. We will suffer during a recession only if we avoid the warning signs and do not prepare. We cannot stress enough how important it is to start and maintain a budgeting and saving habit as this may be your best bet. Review your savings habit and if possible, increase the amounts you put away.