MarketWatch GUIDES

6 Recession Savings Tactics To Protect Your Finances

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Economic downturns happen, but having a budgeting plan and using proactive savings strategies can help shield you from financial pitfalls

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Our Research Process

In This Guide

Defined as a sustained period of slow economic growth, a recession affects nearly everyone, from rising unemployment and slower production and sales to stagnant wages. Here are some key steps you can take to prepare yourself financially and insulate your savings as much as possible before and during a recession.

Key Takeaways

- Setting financial goals early and having an emergency fund are two crucial elements to protect your finances during a recession.
- Speak with a financial advisor about ways to diversify your savings so you can be ahead of the game.
- Look for alternative ways to add income and how to cut expenses as part of a budget plan.
- Look into a high-yield savings account or certificates of deposit that pay a competitive annual percentage yield to make your money work for you.

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1. Build and Maintain an Emergency Fund

Establishing an emergency fund provides a cushion against any loss in income during a recession. Whether you've been laid off or sales at your business are flat, an emergency fund can mean the difference between getting through a tough time and getting into debt.

It's generally recommended to save between three and six months' worth of your living expenses in an emergency fund, although that's just a guideline. Keep in mind that living expenses include more than just your housing payments. Utilities, car payments, food, internet and phone expenses are all likely part of your basic expenses. Also, there are insurances, tax payments and other financial obligations you can't easily pause if your income changes.

If you haven't yet started an emergency fund, or the one you have could use some bolstering, here are some tips for building an emergency fund quickly.

1. **Make a budget**: Take a holistic view of your finances to be sure you have a clear picture of your expenses versus your income.
2. **Identify opportunities to reduce unnecessary expenses**: The less you're spending, the more you'll free up to put toward a savings fund.
3. **Tackle debt where possible**: Carrying high interest debt such as credit card debt or private student loan debt can make it challenging to save money. Consider strategies to help reduce those financial burdens.
4. **Start small**: Putting anything aside, even $20 per month, is better than saving nothing.
5. **Open a high-interest savings account**: A high-yield savings account or high-yield CD can make your money work harder for you.

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2. Reduce Expenses

Look for areas in your discretionary spending where you can save without cutting back completely on things you enjoy. If you have multiple streaming services, for example, consider cutting back to just one. Borrow library books instead of purchasing them outright or paying to download them. Find ways to stay fit through an online fitness service instead of a gym membership. Everyone's circumstances are different, but looking for ways to cut costs and save money without feeling deprived is crucial for your mental wellbeing.

Your fixed expenses may have some wiggle room as well. You may not be able to reduce your rent or mortgage, but you can, for example, ask your providers for a better rate or plan for your cell phone or internet. Carving out the funds to build savings means prioritizing essential expenses over nonessential ones.

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3. Manage and Reduce Debt

Paying down debt should be a primary goal entering into or in anticipation of a recession, as you may end up experiencing hardships that could make it difficult to pay it off and find yourself in a deeper hole.

Two of the most popular approaches to paying off debt are the debt snowball and the debt avalanche methods. With the debt snowball method, you focus on paying off the smallest balance first while making the minimum payments on your other debts. When that balance is paid off, you move onto the next smallest balance and roll the payments from the now paid-off balance to the next one. The idea is that you gather momentum and a psychological boost as you watch the debts decrease.

With the debt avalanche approach, you focus on paying off the debt with the highest interest rate first — regardless of whether or not it has the highest balance — and repeat with each successive debt. This approach will save you the most money on interest over time, but the best choice between the two is the one that motivates you the most.

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4. Maintain and Increase Savings

Realistic expectations are important when it comes to your savings goals in a recession. If your income is reduced, you likely won't be able to save as much. If you're receiving a steady paycheck, consider automating your savings by setting up a set amount to be taken out of each paycheck and put into your designated emergency savings account.

Some banks or personal finance apps may offer round-up programs where you have your purchases rounded up to the nearest dollar and the difference is automatically deposited into your savings or investment account.

The type of savings account you want to use can also help increase your savings. High-yield savings accounts give a great return but may have withdrawal limits or requirements to earn the top rate. CDs might have competitive rates, but most charge an early withdrawal penalty if funds are removed before the maturity date.

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5. Diversify Income Sources

One way to protect yourself if you anticipate a drop in your main source of income is to develop other ways of making money. Depending on your particular skill set, you could look for freelance or part-time opportunities via LinkedIn, Fiverr or similar employment websites. You could also consider working a side hustle.

Longer-term options could include buying a rental property or developing a part-time passion into a larger endeavor, such as marketing your services or buying all or a piece of a business. The more income streams you can create, the less dependent you'll be on any one source of income that may be reduced in a recession.

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6. Long-Term Financial Planning

Having multiple revenue streams can help mitigate the effects of losing a job or having your income reduced. Similarly, keeping your investments in a mix of lower-risk investments (such as bonds and treasuries) and higher-risk growth investments (like stocks and mutual funds) can help balance changes in an unstable economy.

There's no guarantee you can have a recession-proof portfolio, and each person's ideal investment mix depends on their own unique financial situation. But a financial planner can help you decide the right level of risk and growth and tailor an investment strategy to meet your needs.

"The most common response to a recession is to overreact," said R.J. Weiss, certified financial planner and founder of The Ways To Wealth. "Every recession is different, and the assumption is that this is the new normal. However, when investing, the problem with overreacting is that you must be right twice. You need to sell before the market goes down and then buy back in before the market goes up. This is the exact opposite of most people's natural tendency because markets are at their lowest point when confidence in the market is the lowest."

With investing, keep in mind that recessions and recovery are cyclical, and a downturn in the financial markets will eventually revert to growth. Maintaining your investments, including any retirement accounts, and avoiding panic selling will help your holdings appreciate with the right mix and guidance from experts.

FAQ: Recession Savings Tactics

How much should I have in an emergency fund during a recession?

How can I reduce my expenses effectively?

What strategies can help me manage debt during a recession ?

If you have feedback or questions about this article, please email the MarketWatch Guides team at editors@marketwatchguides.com.

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