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Meltdown Gives Consumers A New Money Mindset

A New Frame Of Mind: Meltdown Has Led Consumers To Take Control Of Their Money Matters

(AP)

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(AP) If the Great Recession has taught people one thing, it's this: They need to take charge of their finances.

It's a lesson plenty are heeding. People are saving more and spending less. The personal savings rate has risen to more than 4 percent after sinking to near zero in the months before last fall's meltdown. The number of people getting financial counseling is 3.2 million, double the amount two years ago.

In ways big and small _ from scrutinizing their bills and joining credit unions to scaling back weddings and college plans _ people are finding creative ways to deal with the worst recession in a generation. In short, there's a quiet revolution taking place in the way people save, borrow and spend that represents a retreat from old habits, and the first steps toward new ones.

SAVING

For years, the traditional savings account has been a quaint relic of the past. There were just too many other things to do with our money _ and most involved spending it. Home improvements _ and, for many, a second home; a second car and then a third; overseas vacations. The list went on. Saving meant putting money in a 401(k), and many didn't put as much into those as they could. Then the market plunged and the value of those accounts fell with it.

Now, many people are reassessing their approach to socking money away.

While personal income is down slightly since the recession officially began in late 2007, the personal savings rate is rising. In 2007 the savings rate stood at 1.7 percent of after-tax income. That climbed to 2.7 percent in 2008, and in July _ the most recent data available _ hit 4.2 percent. As people fear losing their jobs, they will save more: Economists expect the savings rate to top 6 percent in coming months if unemployment _ which was 9.7 percent in August _ continues to rise.

But people are still saving less than they did in the last major recession in 1982. Back then, the savings rate was 10.9 percent when certificates of deposit were earning more than 12 percent.

These days, it's difficult to earn much on savings. Most bank money-market accounts offer a return of less than 2 percent, and even long-term certificates of deposit offer little more than 2 percent.

Reducing credit card debt can be one of the quickest ways to save. With credit card companies charging more than 13 percent on average _ and up to 30 percent for people with poor credit _ reducing or eliminating that monthly payment will save money.

Financial planners used to advise consumers to save enough money to cover their expenses for three months. When the worst of the recession hit, Laurie Siebert of Valley National Advisers in Bethlehem, Pa., already was advising clients to boost their emergency savings to six months. Now, she's urging them to save enough to cover a full year of expenses because credit lines and job security aren't guaranteed.

One big reason to save more now: Homeowners can't depend on rising property values to refinance their mortgages to help cover household expenses.

People are flocking to bank and money management Web sites to compare interest rates and share advice. Traffic to personal financial management Web sites, where users can analyze their saving and spending, has soared. The largest site, Mint.com, saw traffic grow from 200,000 visitors a month in January of last year to more than 1 million a month this year.

Smart consumers treat their savings as an expense and set aside their savings before paying other bills. When the bills are paid off, they shift that money into a savings account.

And if you're not participating in your company's 401(k), start now. If you are and don't save as much as you can, increase your monthly contribution. Remember that you can borrow money to help send your kids to college, but there aren't any loans for retirees.

BORROWING

Credit isn't as easy to get anymore, so people are getting creaive to find new sources of funds.

Bank loan balances declined by 4.6 percent for the year ending in June. But credit union loan balances rose by 4.5 percent, according to industry associations. Credit unions _ which are nonprofits and weren't as tangled in subprime mortgages _ are in better shape to make consumer loans.

Borrowers also have begun to explore less-traditional options. The credit crunch helped fuel the growth of what's called peer-to-peer lending, in which companies enable individuals to make loans to one another. One of these startups, The Lending Club, issued 446 loans worth $4.3 million in August alone. That's more than eight times the $488,600 in loans the company issued the same month two years earlier. Virgin Money, which facilitates loans between family members and friends, saw its loan volume more than double to $425 million in June from $200 million in October 2007.

Though new options have emerged, the subprime mortgage crisis laid bare the reality that easy credit can be dangerous. Over the past year, the government stepped in with tighter regulations and is now considering a new consumer agency to protect people from shady mortgage lenders, abusive credit card fees and other risky financial products.

Many cardholders, meanwhile, have been surprised to see their credit limits cut. Credit card companies slashed limits for 58 million cardholders, or about a third of consumers, in the 12 months ending in April, according to a report issued last month by FICO, the company that produces the most widely known credit scores. A majority of the cardholders had good credit scores when the cuts were made.

Gloria Womelduff says Chase recently lowered her limit to $7,500 from $10,000, even though she says she's never late on payments and always pays more than the minimum.

"I'm as squeaky clean as you can get," says Womelduff, 56, a hospital research coordinator in Kansas City, Missouri.

New credit card regulations should mean that fewer consumers are caught by surprise. In the months ahead, revamped billing statements will calculate the interest cost of making only minimum payments and show how long it would take to pay off the balance. For many, both numbers may be a shock.

The statements aren't required until February, but borrowing has already grown more prudent. The Federal Reserve says revolving credit _ made up primarily of credit cards _ declined by $6.1 billion, or 8.1 percent on an annualized basis, in July. That was part of a record $21.6 billion retreat in overall borrowing.

There are some things consumers can do to protect their credit: They can pay bills on time and review their credit report at least once a year. Plus, whenever they're using credit, they can factor the cost of the loan into the budget _ weighing whether the money spent on interest could be better used elsewhere.

SPENDING

People are saving more and cutting their debts. But at some point, they'll start spending more. Businesses big and small hope so. What's emerging so far, though, is a more prudent consumer.

The use of coupons soared 19 percent in the first six months of this year vs the first half of 2008. People are reading bills more closely, looking for mistakes and to identify unused services that can be eliminated. Legions have sought help online. BillShrink.com allows users to compare the cost of cell phone plans and credit cards, based on actual usage. Visits to the site have grown more than tenfold since the start of the year and hit 650,000 in August.

The changing behavior can be seen in other ways:

_ Two years ago, the average amount spent on a wedding was $28,000, according to the Wedding Report, a market research company in Tucson, Ariz. Last year's average: $21,800. The second quarter of this year: $16,550 _ 42 percent below the 2007 average.

_ While enrollment numbers aren't yet available, public colleges reported a 14percent spike in applications last spring, suggesting some students and their families are shifting from private schools so they can spend less.

How to spend wisely hasn't changed because of the Great Recession. The rules were just ignored during the good times. They start with creating a budget to project income and expenses and guide spending. They examine the financial plan each month to find ways to cut back _ whether services that aren't needed or fees that can be avoided.

Smart consumers also take advantage of all employee benefits; use a flexible spending account, when available, to pay for child and health care costs; and review insurance policies to make sure they're only paying for what they need.