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A downturn with a difference

Current economic slump is similar to others, but 401(k), IRAs and feds complicate matters

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Economic downturns are all alike, according to Frank James, founder and chairman of James Investment Research in Xenia.

"Severe economic downturns almost always start the same way," James said. "Too much enthusiasm about the future, too much borrowing, too much debt. The debt becomes hard to service, leading to contraction.

"The present downturn occurred when national debt rose from twice national income before the 1980s to five times in 2007."

James said that, at the same time, personal savings declined from 10 percent of disposable personal income before 1980 to near zero two years ago.

The only difference James sees between this downturn and those in the past is what the public has an "affection" for.

"The fad this time was residential real estate," he said. "Houses are very expensive, take many months to construct and are hard to dump. They peaked in price nearly two years ago. Today home prices are 27 percent lower and are still declining in price.

"Worst of all, the government decided to intervene in the market," James continued. "This had the effect of slowing the decline in prices, of confusing and scaring potential buyers by constant changes in the program. These actions did not permit prices to reach a point where the markets would clear."

Marge Forrester, CFP, an adviser with Ameriprise Financial, also sees similarities between past recessions — such as the one in 1973-74 — and today's downturn, but also a distinct difference.

"People now have investments in 401(k) plans and IRAs that are in the market," she said. "These were not available in the '70s."

Forrester recommends developing a plan for recovery.

"I like to start with a financial plan and look at two categories: Money to live by and money to grow by," she said. "A plan that will have strategies to handle not only investments, but to prepare for the unexpected and rough times you may experience as well as the golden times."

James said "the kind of contraction we are in today will work out to be more severe than any since 1945, so they (business owners) should not count on an early recovery. Owners should work to reduce debt and build savings."

Specifically, James said business owners should refinance debt at today's lower prices. He expects higher inflation and thus, higher interest rates as the Federal Reserve "monetizes" the national debt. He also recommended exploring opportunities for exporting since the coming cheaper dollar will help sell goods overseas.

Finally, he said, business owners should address staffing.

"A very large pool of talented, well-educated people is available to fill vacancies and lay the foundation for future growth."