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Protecting Your Family's
Finances During an
Economic Downturn

Many economists are predicting that the US economy will experience a downturn, if not a recession, in 2023. A downturn can lead to job loss, reduced income, and financial insecurity. While it's impossible to predict the future with certainty, there are steps you can take to protect yourself and your family from the potential effects of an economic downturn.

Update your financials and create a budget.

Now is a great time to update your financials and create a budget. Updating your financials will provide better visibility into where you stand financially and shed light on expenses that could or should be cut.

Your updated financials can serve as a basis for creating a budget for at least the next twelve months. Identify core expenses versus non-essential items like entertainment, vacations, and clothing to understand what could be cut without much trouble. Test your model to see what changes you would make if your income were to decrease.

Reduce high-interest debt.

As interest rates rise, the cost of borrowing becomes more expensive. Review your debt and the associated interest on each account. Prioritize paying down the most expensive debt first and consider whether it makes sense to liquidate any investments to pay down the debt. Paying down debt will lower your interest expense, increase your available credit, and potentially increase your credit score.



Bolster cash on hand and maintain available credit

A recession can lead to reduced income, but for business owners, it can also lead to cash calls. For this reason, it's important to maximize your cash availability.

Ideally, families should have savings that can cover three to six months of expenses if needed. While not all families have that much in savings, having available credit can help. For this reason, avoid closing any credit card accounts or lines of credit that may be needed in the future. If you feel that additional credit would help during a downturn, then secure the credit now prior to a downturn.

If you're a business owner, consider whether or not your business may need cash during a recession, and if so, how much. Unfortunately, business owners often serve as the backstop for their company's financial needs, so it's important for the owner to secure a line of credit or build cash reserves at the corporate level to help protect them personally.

Take stock of loans, personal guarantees, and debt covenants.

If you have personally guaranteed any loans or if your business has a loan, review the terms of each loan, the outstanding balance, the borrower's ability to pay, and the amount of your guarantee. Review any debt covenants attached to each loan and where the borrower currently stands in regard to requirements. If a loan falls out of compliance, you and or your business may be required to pay down some or all of the loan.



Protect your personal assets

Having an estate plan is critical to protecting and maximizing your assets for you and your beneficiaries. If you don't have an estate plan already, then now is a great time to consult with an advisor to create one. If you do have one, then review it to identify any updates or changes that need to be made. If your estate plan includes a trust, make sure it's funded, and assets are titled correctly.

If you own a business, it's important to keep your business assets separate from your personal assets. For instance, do not co-mingle personal and business funds in the same bank account, and if you own multiple businesses, be careful about co-mingling their assets. Co-mingling assets can create undue exposure to risk and legal and tax issues.

Many estate plans include the use of an irrevocable trust for both tax benefits and asset protection. When assets are put into an irrevocable trust, the grantor gives up legal ownership of those assets. The assets are no longer considered part of their personal estate, which provides certain protections from creditors. However, irrevocable trusts are not for everyone. Once created, the trust cannot be changed or revoked without the consent of the beneficiaries. Also, they are usually managed by an independent trustee, meaning the donor must give up certain control over their assets.

Asset protection strategies are only effective if they are performed within the confines of the law. This means you should not attempt to avoid debts by swiftly transferring assets to another person or entity when a lawsuit is looming or underway. Doing so could be considered a "fraudulent conveyance," and you could face legal repercussions and lose any asset protection you attempted to obtain. The best way to avoid a fraudulent conveyance is by protecting your assets at a time when you are financially stable, long before any lawsuits or creditor claims arise.



Final Thoughts

This document is intended to provide strategies that will help you and your family prepare for an economic downturn. It is not a substitute for speaking with one of our expert advisors and is in no way meant to provide any legal advice. Every situation is unique, which is why it's important to consult with our expert advisors about your specific situation. If you'd like to learn more, please contact our office.



About Cain Ellsworth.

Cain Ellsworth is not all things to all people. Instead, we specialize in serving small to medium businesses in banking, manufacturing, property and casualty insurance, plus a variety of other industries. And we dedicate significant resources to assure that we are well-informed in each of them.



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