

Remember hard-earned financial lessons of 2008

By Eileen Ambrose
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What investor wouldn't like to forget 2008?

It was the worst year for stocks since the 1930s, and there seemed to be no place to hide.

But as much as we would like to put last year out of our minds, we should look back to see what we can learn from it. It might prevent us from repeating our mistakes.

Among the lessons:

Keep a cash cushion. As the economy weakened, [T. Rowe Price](#) noticed an increase in workers asking for hardship withdrawals from the 401(k)'s the company administers.

"It didn't take a cataclysmic event" to push them to that point, said Stuart Ritter, a T. Rowe Price financial planner.

In fact, the workers didn't have excessive debt, weren't living beyond their means and didn't have ridiculously big mortgages, he said. But they didn't have an emergency fund to tide them over during a setback.

The traditional advice is to keep three to six months' worth of living expenses in a savings or other cash-like account, although some job seekers are finding that it takes longer than that to find work.

[Colorado](#) financial planner Amy Noel said she now advises people to set aside a year's worth of living expenses for emergencies or three to five years if they are retired.

Stocks are for long-term money. One problem exposed by 2008 is that many people, even retirees, had money in the stock market that they were counting on to spend soon.

A few years ago, the rule of thumb was that money you needed to spend within the next five years should not be in the stock market.

In recent years, many financial advisers are becoming more aggressive in that thinking. Some said money needed in three years shouldn't be in the market. Then it was two years. Then one.

Their reasoning: You need the growth that stocks provide to keep up with inflation, something savings accounts just can't do.

Even retirees need to be in the market, considering that their retirement could last 30 or more years. But only money not needed for many years should be in stocks. The five-year rule is a good one.

Past isn't future. The impulse is to look at the recent past and assume that's the wave of the future. That's why investors tend to pour money into the stock or mutual fund that performed the best the year before.

But one year isn't a trend, particularly last year, when even well-diversified portfolios lost money, said **Chuck Carlson, chief executive of Horizon Investment Services** in Indiana. This could lead investors to wrongly conclude that diversification is dead. If you have a diversified investment strategy that has worked well for years, don't abandon it "based on a year where nothing worked," he said.

Live within your means. Easy credit disguised the fact that so many people were living on the edge. Many consumers also confused a bank's willingness to extend credit "as an indication the lending institution thought they could pay it back," said New York financial planner Gary Schatsky.

The lesson here is to live within your means and not take on debt that you can't afford to shoulder.

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