

EPISODE 1371

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[INTRO]

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FT: Welcome to So Money, everybody. It is Friday, June 17th. How you doing? Farnoosh Torabi here. I know you've got a lot of questions about the economy on your mind. I was on Instagram earlier this week, right before the Fed announcement came down on – I guess it was Wednesday, Thursday. I can't remember now. Yeah, it was Wednesday. We all anticipated a massive rate hike, 75 basis points. That's historic. I mean, it hasn't happened in, I don't know, like 20 years, 30 years. 1994. Am I dating myself? I was 14 years old. So, yeah, like almost 30 years. Yikes.

I have those questions now. We're going to get to your big questions about what to do with your investments. Should you save differently now? Should you pay down debt differently? Like how is this rate hike, 75 basis points, which happened on Wednesday, going to trickle down to your bills? So I have some important advice coming up in the show. But first, let's talk about this rate hike, right? Like what does it even mean when the Federal Reserve raises interest rates?

Back in the day, I was a reporter for NY1 News, a producer, actually. Well, I was a producer and a reporter and a shooter and a booker and like get your coffee girl. I did it all because that was – We were nonunion, and it was kind of great. But I remember, every, I guess, FOMC meeting, which was not every month, but it was like every few months, when the Fed would meet, the Federal Open Market Committee. That was my job. I was supposed to watch and go live with the Fed interest rate.

A lot of times, like they did nothing. But the moments, the times when they would do something. It was always very rattling, and the stock market would go crazy a little bit, and that's what we saw, right? The morning after the Fed rate hike, the markets tanked. The Dow fell like, I don't know, 500, 600 points. I don't know where it closed, but it was a pretty bad morning. So those moments kind of give me a little bit of – They trigger some trauma in me because they were very nerve-racking times, and I was very green, and I had to learn a lot on the go.

But now, I have those years behind me, and I have some perspective, and I have this podcast to share those ideas with you. So what I can tell you very simply is that when the Federal Reserve looks at the economy and sees inflation go crazy, like it has been, it is its job to temper that, to control inflation. That's their number one job is to manage inflation and keep it at more like 2% versus where we're at now, which is like four times that, more than four times that.

How do they do? They control monetary policy. That's their thing. How do they – What does that even mean? It means, well, they're managing sort of the economic health. To do that, they either raise or lower interest rates to sort of manipulate how we, as consumers, spend. Right now, inflation is really high. They want to cool that, so they want to lower spending. So they raise interest rates because the theory is that by raising interest rates, we will be less motivated to go out there and borrow money, whether that's on our credit cards or take out a mortgage, take out a car loan to finance our lives that we're going to maybe be more inclined to save.

Why do interest rates go up when the Fed raises rates? Like what's the process there? So the Fed is actually raising this overnight bank lending rate called the Fed funds rate. So when banks have to pay more for interest, that means we have to pay more for interest. They're not going to let us get away with it. So then that trickles down into their financial products, including those savings. Savings will also go up. So I guess there's a balancing act here.

The Fed is doing this 75 basis points, which is .75% is the largest hike since 1994. I think that it is appropriate. Is it going to be the silver bullet to get us out of inflation? No. Chairman Jerome Powell said as much. He said we're going to probably do this again next time we meet and maybe again later this year. That's going to, again, have trickling down effects. It could lead to a recession if we're not already in one because when spending slows by consumers. It's not just

consumers. It's also businesses. Businesses also have to pay more interest for their loans. So they may, in turn, start the layoffs.

We've already seen layoffs across the market. Particularly, I've been seeing a lot of layoffs in the tech space. There's this website called layoffs.fyi. In June, which we're only halfway through the month, they have logged, I don't know, something like 60, 70, corporate layoffs. A lot of these are startups, but a lot of them are also big companies that we know, and that compares to what we saw in May, the entire month of May. We saw about 60, 70 corporate layoffs and already midway through June, where we were for the full month of May.

I think we're going to see a very different jobs picture in a couple of months, and what I'm also seeing too is this is going to, anecdotally, companies laying people off by giving them severance for however many weeks, sometimes months. So we're not going to see those jobless benefit applications start happening until later. There's going to be a little bit of a lag. Right now, we think, "Oh, the job market is so rosy. Why are we raising interest rates? Well, there's no way we're going to go into a recession."

From where I stand, and people tell me everything, I'm seeing a lot of the opposite. I'm seeing people losing their jobs. We know that people have slowed down spending because Target and Walmart have told us. Their earnings reports were not rosy, and their forecasts for the year were revised lower. Consumer sentiment is down. So we know that while inflation hasn't quite cooled, the economy is cooling. People are not feeling great. People are hurting. So I think with the next month's GDP report, which is we talked about earlier on the show, two consecutive quarters of GDP decline is a technical recession.

We had one quarter already showing a little bit of a dip in GDP. I think we're going to see similar news in July when we read the second quarter report. I don't know. I think I would bet like \$5 that we're going to look back and say, "Okay, we were already in a recession. The recession has arrived." But anyway, not to scare you, this show is here to help and to inform and to find those silver linings, although, I'll be honest, it's really weird to talk about silver linings at a time when everybody is hurting to some degree, some more than others.

With that, with that lovely transition, let's talk about what's on your money mind. Okay, let's go to the mailbag and answer your financial questions. As I said, this was just like a casual – I popped it on Instagram. So if you're not following me there, please do. @farnooshtorabi on Instagram. I'm supposed to also be getting on TikTok eventually. Fingers crossed for that journey. But I just asked. Drop me a question, and I got a flurry of questions. So here we go, without wasting any more time.

We've got a question here from Megna. Maybe it's Megan. Your Instagram handles are very creative, I have to say. So apologies if I am not pronouncing them correctly or if I'm not getting the joke. Her question, "Will the recession have an effect on my outstanding credit card bills?" The short answer is yes. If you are carrying a balance on your credit cards currently, then you will likely see an uptick on your interest rate within the next two to three billing cycles. That's usually the speed of how long it takes when the Fed raises rates, when we're going to actually see that appear on our credit card statements.

I would say that if you have some outstanding high interest credit card debt, prioritize it. Make an extra payment or two. Pay more than the minimum. Look at the year and say, "Okay, if I want to be debt-free this time next year." We know rates are going to continue to go up. I want to reduce that burden of interest, and I want to be debt-free as soon as possible. What is it going to take to be debt free in a year and reverse engineering? Our credit card statements, actually, by law have to tell us what we have to pay every month to be debt-free in three years, five years. So use those benchmarks to help guide your goal.

The question is will the recession have an effect on my outstanding credit card bills. The answer is it's less about the recession. It's really about interest rates, right? As interest rates go up, it's all like a journey, right? As interest rates go up, the economy cools. A recession is likely how deep or severe it is. We don't know how long it's going to last. We don't know. So it's less about what happens in the recession. It's more about what happens with interest rates.

At some point in a recession, as we are sort of seeing inflation come down, interest rates will also hopefully come down too. So I wouldn't be less worried about, well, if there's going to be a recession. What we do know is that interest rates are going up. To protect yourself in that environment, it's really important to the best of your ability just prioritize, especially not just credit

cards, but any loan you have that has a variable adjustable rate. So that could be your private student loan. That could be, I don't know, your HELOC that you've drawn down on, and that's adjusting higher as we see the Fed raise rates. So Megan, thank you for your question, or Megna. That might have also been my – I may have transposed that incorrectly.

Next question, CGXXII, 22, I guess, in Roman numerals. What is better to buy, excuse me, during a bear market, ETFs or single stocks? So we are in a bear market. Now, let's pause for a second. What the heck is a bear market? Well, technically, the definition is when the major indices are down 20% from their highs, which we have seen, right? Whether you're talking about the Dow, the NASDAQ, these are major industries that track different kinds of markets.

The Dow tracks the major industrial companies and sort of like these Bellwether companies, the McDonald's, and Microsoft of the world. Then you have the NASDAQ, which is very tech-heavy. Sometimes, Dow stocks also appear on the NASDAQ. But the NASDAQ is really a benchmark of like the tech market, which is a lot of our market these days. Those indices are down 20% off their highs. So we're in a technical bear market.

But my advice for how to invest in this market is the same as it would be how to invest when things are rosy, when we're in a bull market. I always like to say, and the guests on the show, we had a bunch of guests on in previous weeks, talking about how to think and act in this market. Low-fee, index funds or ETFs that track the US stock market will get you quite a diversified portfolio, quite a diversified exposure, right then and there. It's never really out picking individual stocks.

Because when you pick an ETF, you're effectively picking individual stocks. The ETF is doing it for you. Your time is not wasted, and we all know that cherry picking stocks is like throwing darts. So let the algorithm do it for you. Let the experts who are putting together these nice ETFs low-fee do that for us. I don't really have a stock picking strategy, whether in a good market or in a bad market.

To recap some of the advice that has been shared right on this podcast in recent weeks about how to think about the market, one that I love is from Adam Cecil, who wrote an important book recently about how to think like a future trader, like a future investor, which is kind of like how

he's always been preaching, which is that you can't time the market. But your timing in the market, like the amount of time you're in the market, is more important than whether you get in on a Saturday or on a bear market or June, right? It's like get in and stay in.

We have more questions in the run up here about like what are you doing with your portfolio. Should I like adjust my portfolio? I'm going to get to that in a minute. Here it is. Look. Look, it's Manny. Look, it's Manny. What are you doing with your stocks? Are you getting out? No, I'm not getting out. But I will say this, and I'm going to be very honest with you. A lot of experts will say just ignore what's going on. But if you really are losing sleep at night, if this is panic-inducing for you, if you can't stop thinking about it, maybe there's more to this than we're acknowledging. I don't want to dismiss the mental health crisis that can evolve around something that is pretty scary to see your portfolio down 20%. That's not a little thing.

So I want to recognize that and just say this. That I'm not saying make a knee-jerk move. I'm not saying go in and start moving things around. But I will say that, for me, at least, two years ago, when COVID had just been announced, and the lockdown had just happened, and the market in March was tanking day after day after day after day, and I just put a bid on a home, and I'm the breadwinner in my marriage, and I've got two kids in school, and I thought to myself, "I'm going to look at my portfolio," because I was losing a little bit of sleep.

I'm going to be very honest with you. I was like, "My portfolio is down quite a bit, and I want to take a look under the hood." I'm not going to do anything rash, but I just want to see how much exposure do I have to stock because it's been a while. So if it's been a while for you to look at just your allocation, how much of your portfolio is in stocks versus bonds versus cash, there's that rule of thumb. Take 100 or 110 now and subtract your age. That's the target number that you want to be in stocks. The rest you put in things like fixed income and bonds and cash.

I was 40. So even if you take 110 and subtract 40, what does that leave you with? 70% in the stock market. I was like 90% in the stock market. So, yeah, my risk tolerance, my appetite for risk was just not there anymore, and that's fair. We create these portfolios at a young age sometimes, and then life happens, and we just kind of like move on. Yes, the algorithms will adjust for us, usually, as we age to reduce our risk exposure. But it's still a very personal target, right? It's a very personal question. How risk-tolerant are you?

I thought to myself, right now in my life and moving forward, I don't have a 90% stock exposure, appetite for risk. You know what I'm saying? So I did go back to the platform where I was investing, the robo-advisor, and I retook the questionnaire, which you always can take to make sure that your portfolio is aligned with your risk tolerance. At the end of that questionnaire, it was determined that I should be more like in the 70 to 80 percent range invested in equities versus bonds.

So we did make that little tweak, and I felt better about it, and it was a long-term adjustment that I made. It wasn't like, "Oh, that's how I felt on Tuesday. I made the switch." Then Thursday, I got second thoughts and did something else. No, no. This was like a very thoughtful sit down, reevaluation. I spoke to some financial experts who are smarter than me, and I proceeded with what I did.

I think this is a little contrary to what we hear out there, which is like ignore what's going on, do nothing. I think if you're just starting out, and you're 25 years old, and this is like your first year investing, and you are diversified, yeah, don't worry. But if your life's evolved, if you're in midlife, if you're approaching retirement and your portfolio is tanking, then I do believe in the cyclicity of the market that what goes down goes up and vice versa. There are actually more bull markets than there are bear markets, and the bull markets last longer than the bear markets historically. So let that give you some confidence.

But I do think there is some value in just that exercise that I did, which was to kind of go through that allocation. Am I okay with this risk exposure to the stock market? Not just because right now I'm looking at CNBC and what they're saying and, oh, my god, I'm scared. But because my life circumstances have evolved, my appetite for risk moving forward is different, and my portfolio should reflect that. If you can talk to somebody who can give you a little bit of perspective and expert advice.

That was a long answer to a pretty short question, which is what are you doing with your stocks. But I really wanted to expand on that, and I want to address the mental health component to all of this. That, yeah, it's a really nerve-racking time for many people, myself included at times.

Mary Grace Gardner, she's an avid listener, and I love her. She says, "My dad just retired and is seeing his retirement plummet. What should he do with his portfolio?" So I just finished talking about the importance of reviewing your allocation. Might your dad be too exposed to the stock market right now for his life stage and for his financial needs. Like if he's, let's say, 65, and he's 80% in the stock market, I might revisit that. Okay.

One other thing I'll say about those who are approaching retirement or are early retirees, meaning like they just arrived in retirement, and I'm not talking about like 40-year-olds who are on the fire journey, but like you're normally retiring at 65, what have you, and you're noticing your portfolio really take a nosedive. I would look and see how your portfolio is being invested because there was a study that came out not too long ago. I read about in the Wall Street Journal, where – Or maybe it was MarketWatch. I can't remember now the source, but essentially it was this. Target date funds, which I'm sure we all have, if we are investing in a 401(k) or just like broadly investing, there's probably a target date fund in the mix. Or maybe that's all we're invested in.

What is a target date fund? It's essentially a mutual fund that targets your projected retirement date, and the algorithm within that fund sort of mirrors your journey and your risk tolerance and your timeline to make sure that you're allocated appropriately. That, again, if you're 50, your exposure to stocks is appropriate. But what we're finding or at least what this study found was that these target date funds may still be too aggressive, particularly for those who are approaching retirement.

Look at that and, again, talk to an advisor. If that is the case, maybe you dial down your exposure. Or maybe you move the money out of that into a different target date fund, with a slightly more conservative approach to the stocks, a more conservative investment mix. But I wouldn't panic too much. I mean, I remember my father in the '90s dot-com bubble bursting, he panicked and sold all of his stocks. His retirement has done okay in the last – I guess, it's been 20 years. But he's really regretful of the fact that he abandoned his portfolio.

I think even if you're in your 60s, it's not really a time to abandon because, remember, if you're healthy too, your retirement has just started. You're probably looking at another 20, 25 healthy years. In that time period, I'll be willing to bet a lot of money, not just \$5, that your portfolio will

rebound. Those who stuck with the market when it tanked in 2008, 2009, what happened? They experienced one of the longest running bull markets of our history, of stock market history. They did handsomely because of that. Those who abandoned are playing catch up.

Don't panic. Revisit your portfolio if that's really keeping you up at night. Specifically, eye those target date funds. Talk to a financial planner. Maybe his portfolio is being managed by somebody, where you can talk to that person for free and just check in. But remember, retirement is not one year. It's 20, 25 years longer for many people. In those decades, I would imagine that the portfolio would see brighter days, and he's not going to need to pull out all this money at once. He's going to take out his four or five percent and do it incrementally. So even if some of his portfolio is down, it doesn't mean that he can't support himself right now, right?

Megs Chang has a question. I've been conservatively investing my down payment for a home. I'm not planning to buy a house for four to five years. Is this still a good plan? Yes. Rule of thumb, if you have money that you don't want to take out for a little bit of time but not longer than four to five years, I would say keep it in something liquid like low-risk. Maybe a money market fund, a CD, and we've talked about I bonds as well.

The plus side, as we talked earlier, about is that when the Fed raises rates, yes, that means that borrowing costs go up, but also savings yields go up. So this is actually pretty better than average time. I just saw a headline. It was like, "Some banks offering more than 1%." Oh, my gosh. It's time to party. But I think that if you still want to buy a house in fewer than five years, you don't want to gamble that in the stock market. I don't know how long this bear market is going to last or how much longer it's going to take for stocks to rebound.

But I don't think it's going to be in the next year. I mean, if it is, that'd be great. But historically, that's not really happened. So don't risk it. Keep the plan as is. I do think I just saw a headline that home prices are coming down. So you might be able to buy that house sooner than later.

Vanessa, "Do you think a recession that we're close to approaching means that student loans that are currently on hold will go back to being required to repay?" That's a really interesting question. I think you can look at it both ways. I think that it makes sense that if you think we're

going to be heading towards a recession, the economy is going to be hurting, and the government's going to want its money, right.

I actually think the opposite. Maybe I'm optimistic. I feel like if we're in a recession, and people are hurting, and you're trying to get reelected, okay, I don't think you want to piss off your voters and say, "By the way, those student loans that I said you could just pause on, those federal student loans that you could pause on through August, and I also hinted that I'm probably going to extend it, I've changed my mind." I don't see that happening. I do not see that happening. If anything, I do see that the pause is going to be extended as they've indicated.

It's really hard for an administration to go back on their word over something like this, which has been a long time campaign. Finally, we're making some traction. So I am optimistic. I would say that if you have federal student loan payments that are on pause, and simultaneous to that you might have some high interest credit card debt, or your savings isn't really where it should be to help you ride out a potential recession, like we always say, in a recession, cash is power. So traditionally, three to six months is good.

But if you can get up to six months of savings, nine months of savings, if you haven't gotten there, I would do that first. I wouldn't worry about these student loans, which are already being permitted to pause on. So take advantage, and we'll cross that bridge if they go back on their word, on their hint rather. I don't want to say it was a promise, but I have read, and they have said that they plan to potentially extend the ongoing student loan pause. Let's keep our fingers crossed.

That's our show, everybody. Thank you so much for tuning in. Next week, we have very special episodes dedicated to the racial wealth gap. We've got multiple episodes with some incredible speakers. I hope you'll stay tuned and Happy Father's Day to all of our dads out there. Congrats to all the kiddies, kiddos who are graduating from – My kid's graduating from preschool, and I got another one finishing second grade. It's a fun month in our household. So thanks for joining me, and I hope your weekend is So Money.

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