Report for August 2014

Issued August 29, 2014
National Association of Credit Management

Combined Sectors

Consistency is generally a positive development when the overall readings have been positive and this is the case for the Credit Managers' Index from the National Association of Credit Management in August, which posted no change from July's 56.8. This marks five months of readings between 56 and 56.8 and given the volatility in the economy as a whole for this period, this stability in credit is a positive signal as far as the rest of the year is concerned.

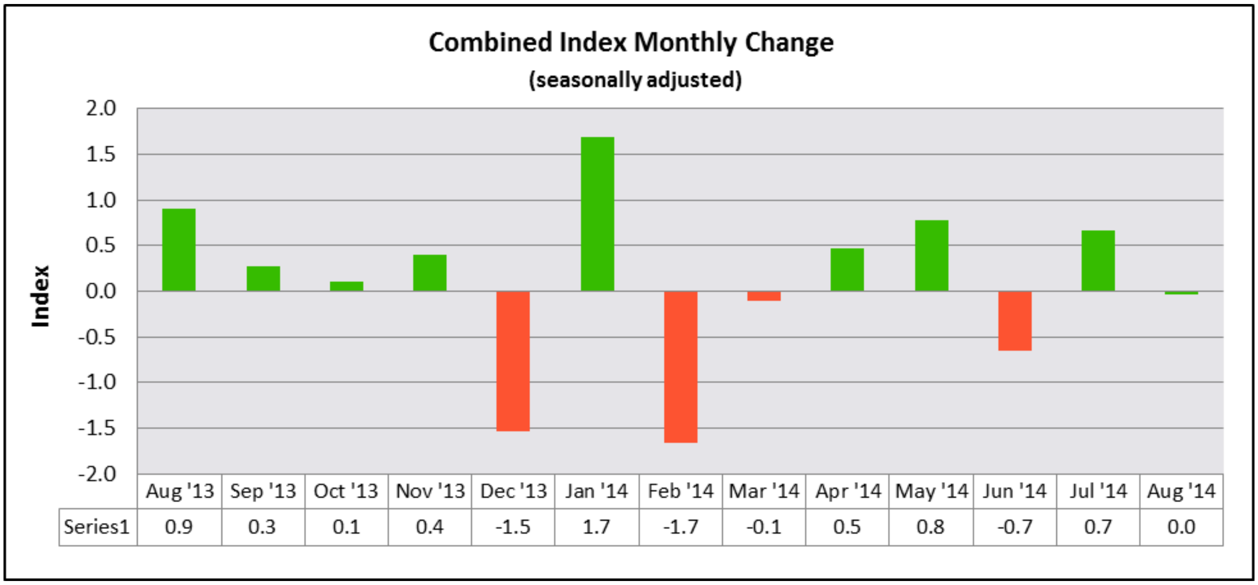
"The August CMI reflects a more optimistic future, but not one that is likely to surge. That should help calm fears of rapid growth sufficient enough to trigger inflation worries," said NACM Economist Chris Kuehl, PhD. Nearly all the index's readings reflect that same stability, though there was noteworthy movement in both the favorable and unfavorable factor indices. Kuehl noted that other important data streams show the same stability—capacity utilization between 78% and 79.7% over this period—just a little shy of what is considered normal. Stability also appears in terms of capital expenditure. "These measures stand in stark contrast to the wild gyrations in the overall growth rate as first quarter numbers were in recession territory at -2.1%, while the second quarter boasted a gain of over 4%," he said.

The favorable factor index improved only very slightly from 63.7 to 63.8. Sales dipped from 65.2 to 64.8, but that is still trending toward the high side as far as the last several months are concerned. There was also a significant dip in new credit applications from 62.4 to 60.9, but it remains above 60. Dollar collections and amount of credit extended both registered gains from 61.0 to 62.7 and 66.1 to 66.7, respectively. This is the second straight month that favorable factors remained in the 60s. Overall, conditions remained strong and pointing toward a better end to 2014 than the start. "In comparing this month's economic data to some of the data reported by the Federal Reserve, it is easier to understand the optimism about the last half of the year, as well as the worry about the impact of inflation fueled by some of this growth," Kuehl said.

The unfavorable factor index was similarly unchanged from last month, but falling instead of rising from 52.2 to 52.1. This consistency suggests that none of the economic concerns that started the year have been sufficiently serious to drag the whole of the economy down. Just as with the favorable readings, there was more movement within the individual factors. Rejections of credit applications slipped from 52.1 to 51.9, seemingly reflecting an increase in marginal companies trying to obtain credit. Anecdotally, reports of more "zombie" companies—those in very bad shape financially, but hoping that credit standards will loosen enough for them to make a comeback of some kind—are making an appearance.

Continuing with the unfavorable factors, accounts placed for collection improved from 51.5 to 52.1—a good signal that fewer accounts are getting into real trouble. Disputes remained stable, rising from 50.3 to 50.6, but dollar amount beyond terms slid from 51.1 to 50.3. This is getting too close to contraction territory for real comfort, but no cause for alarm, noted Kuehl. Dollar amount of customer deductions slipped below 50 from 50.6 to 49.9. That marks the first time for a slip into contraction territory since June. For the last year it has been staying pretty close to the 50 point and will likely bounce back in the coming months. Finally, filings for bankruptcies slipped, barely, from 57.6 to 57.5. "The good news is that the financial distress at the start of the year has not triggered a wave of business failure, and now that seems even less likely," Kuehl said.

Combined Manufacturing and Service Sectors (seasonally adjusted)	Aug '13	Sep '13	Oct '13	Nov '13	Dec '13	Jan '14	Feb '14	Mar '14	Apr '14	May '14	Jun '14	Jul '14	Aug '14
Sales	63.1	62.7	62.5	63.4	58.7	61.5	59.4	59.1	61.8	65.6	63.9	65.2	64.8
New credit applications	58.7	57.4	58.5	59.2	57.2	58.2	58.1	57.3	59.3	58.9	61.5	62.4	60.9
Dollar collections	60.4	60.6	61.4	59.7	58.7	60.9	58.8	56.4	58.1	61.2	59.3	61.0	62.7
Amount of credit extended	63.3	62.9	63.8	63.2	62.6	65.4	61.4	63.1	63.8	65.0	64.8	66.1	66.7
Index of favorable factors	**61.4**	**60.9**	**61.5**	**61.3**	**59.3**	**61.5**	**59.4**	**59.0**	**60.7**	**62.7**	**62.4**	**63.7**	**63.8**
Rejections of credit applications	52.7	53.0	52.1	53.3	54.5	54.6	52.3	52.4	52.3	52.7	52.0	52.1	51.9
Accounts placed for collection	52.5	54.3	53.3	55.0	53.4	55.2	54.6	54.1	51.7	53.8	52.5	51.5	52.1
Disputes	51.6	51.7	51.8	51.9	50.7	52.2	51.9	50.9	54.7	50.2	49.5	50.3	50.6
Dollar amount beyond terms	51.1	52.2	52.7	54.7	49.7	52.8	51.1	52.4	50.0	51.5	49.6	51.1	50.3
Dollar amount of customer deductions	51.4	51.7	51.8	52.4	51.5	51.6	50.4	51.2	50.3	50.4	49.4	50.6	49.9
Filings for bankruptcies	58.7	59.8	59.6	59.0	59.0	60.5	58.5	58.4	58.1	58.4	58.9	57.6	57.5
Index of unfavorable factors	**53.0**	**53.8**	**53.6**	**54.3**	**53.1**	**54.5**	**53.1**	**53.2**	**52.8**	**52.8**	**52.0**	**52.2**	**52.1**
NACM Combined CMI	**56.4**	**56.6**	**56.7**	**57.1**	**55.6**	**57.3**	**55.6**	**55.5**	**56.0**	**56.8**	**56.1**	**56.8**	**56.8**



Manufacturing Sector

The manufacturing sector data seems consistent with information coming from a variety of sources that measure the industrial capacity of the US. There was a very slight improvement in the index from 56.7 to 56.8. As with the combined index, the individual factors showed movement, however, the gains in one category were offset by reductions in another. “The overall sense is that manufacturers are doing well enough and progressing, but there has yet to be a big breakout in growth,” Kuehl said. “This seems partly to do with a reduction in export demand, which seems to be reflected in some weak readings globally in the various purchasing managers’ indices.”

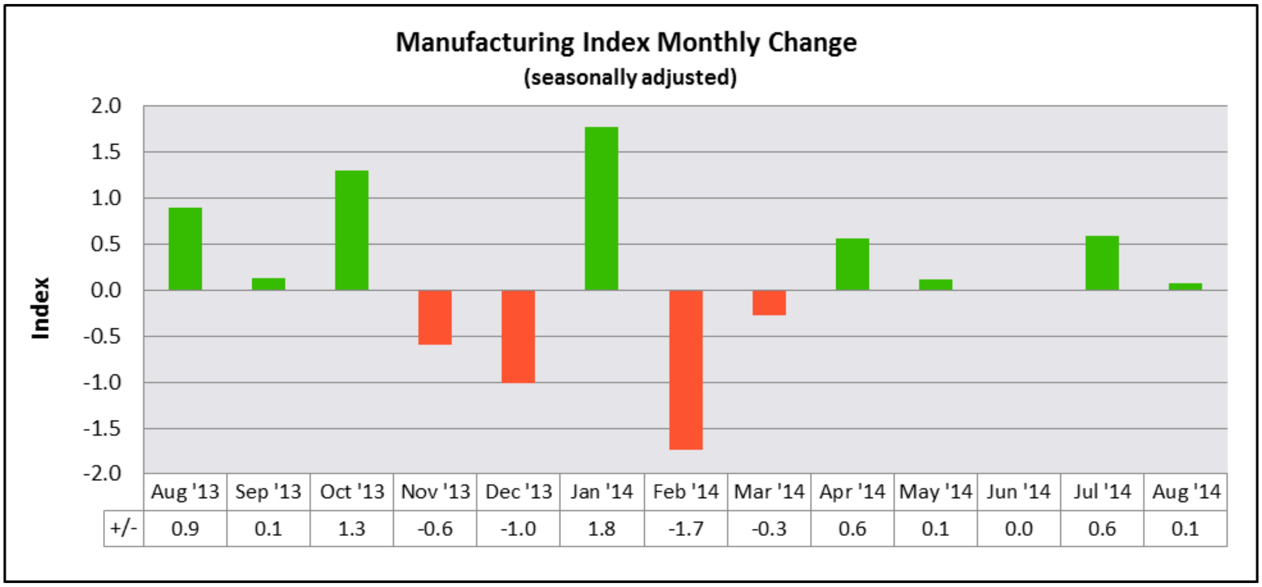
The index of favorable factors improved almost a full point from 63.4 to 64.3. That keeps the index well above 60, where it has been since March. There was some variation within the index, but not much. The best news is that sales continued to rise and now sits at 66.0 compared to the 64.8 reading in July. It is the highest it has been in several years and exceeds the previous yearly high of 65 reached in June. “The drivers of manufacturing demand have been diverse—everything from the energy sector to a still-healthy automotive sector. The growth has taken place even without a healthy export sector and that bodes well for the rest of the year," said Kuehl.

New credit applications dropped slightly from 61.1 to 60.4, but it is still above 60. Dollar collections jumped in the opposite direction, from 61.3 to 64.2. "This is real progress, signaling that companies are getting paid, and on time for the most part," Kuehl noted. "There is good revenue and profit growth in the majority of the manufacturing and industrial sectors." Amount of credit extended was relatively flat, improving slightly from 66.4 to 66.6. Overall, the favorable factors are strong and all very comfortably in the middle 60s for the second straight month.

The readings for the unfavorable factors are also very similar to what they were last month. The index fell from 52.3 to 51.8, with volatility in the some of the factors that accounted for the dip, but nothing too worrisome at this point. Rejections of credit applications dropped noticeably from 52.1 to 51.2, brought on by less creditworthy companies trying to secure access and still getting rejected. Accounts placed for collection slipped as well, from 53.0 to 52.8, but the shift was minor and it remains comfortably above 50. Disputes didn't move, but still hovers close to the contraction/expansion point at 50.3. "This suggests that a significant level of distress still exists in some elements of the industrial community, and that triggers a certain amount of debate," Kuehl said.

Dollar amount beyond terms improved from 51.0 to 51.6. Distress still appears in dollar amount of customer deductions, which fell from 49.2 to 48.5. This is the only factor currently in contraction, and this month's dip erases last month's improvement, although that reading was also below 50. This factor has not been able to dig out of the 40s since April, which is cause for some concern going forward and it does not seem likely that this situation will change much this year. Filings for bankruptcies also deteriorated from 57.8 to 56.3, but nothing truly significant leaving it in a better position than any other unfavorable factor.

Manufacturing Sector (seasonally adjusted)	Aug '13	Sep '13	Oct '13	Nov '13	Dec '13	Jan '14	Feb '14	Mar '14	Apr '14	May '14	Jun '14	Jul '14	Aug '14
Sales	62.3	61.6	64.3	63.4	61.7	59.6	57.9	58.5	61.6	64.5	65.7	64.8	66.0
New credit applications	58.4	55.6	58.9	59.2	57.7	59.5	57.7	56.1	58.8	57.2	61.7	61.1	60.4
Dollar collections	61.0	60.5	61.4	58.7	59.5	62.7	56.4	57.4	59.1	62.0	58.5	61.3	64.2
Amount of credit extended	62.1	62.4	64.8	61.8	61.5	66.4	60.4	61.7	64.5	64.4	65.2	66.4	66.6
Index of favorable factors	**61.0**	**60.0**	**62.4**	**60.8**	**60.1**	**62.0**	**58.1**	**58.4**	**61.0**	**62.0**	**62.8**	**63.4**	**64.3**
Rejections of credit applications	52.3	52.4	52.0	52.9	55.5	54.4	52.8	52.6	52.6	52.6	51.4	52.1	51.2
Accounts placed for collection	53.0	53.7	54.0	55.7	53.3	55.7	59.9	56.1	51.5	53.3	53.5	53.0	52.8
Disputes	49.8	50.8	52.1	51	50.2	51.0	51.6	50.6	57.2	49.6	48.5	50.3	50.3
Dollar amount beyond terms	52.5	52.9	54.6	54.8	50.0	53.2	51.7	52.8	49.5	52.5	50.2	51.0	51.6
Dollar amount of customer deductions	49.3	50.7	51.9	51.4	49.7	51.8	50.4	50.4	48.5	48.3	47.9	49.2	48.5
Filings for bankruptcies	57.9	59.4	59.0	58.5	57.7	60.4	58.6	58.5	57.0	57.1	58.7	57.8	56.3
Index of unfavorable factors	**52.5**	**53.3**	**53.9**	**54**	**52.7**	**54.4**	**54.1**	**53.5**	**52.7**	**52.2**	**51.7**	**52.3**	**51.8**
NACM Manufacturing CMI	**55.9**	**56.0**	**57.3**	**56.7**	**55.7**	**57.5**	**55.7**	**55.5**	**56.0**	**56.1**	**56.1**	**56.7**	**56.8**



Service Sector

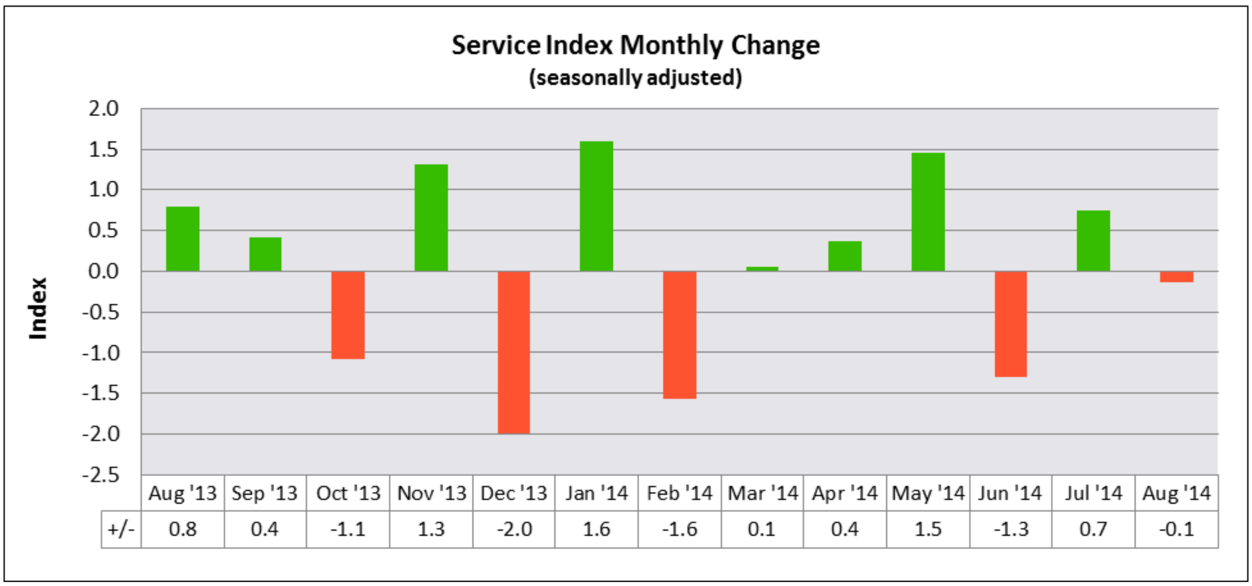
The action in the service sector was no different than in manufacturing—another month that looked similar to the one before. The index fell from 56.9 to 56.7, a slight dip. The important news is that it remains squarely in the middle of the 50s and that is as healthy as it has been tracking for the past year. The variation in the last 12 months has been slight with a high of 57.5 in November to a low of 55.5 in February. Movement was a little more varied in the factors.

The favorable factor index was 63.3, a fall from the previous month's 63.9. More gyration appeared in the factors. Sales dropped from 65.6 to 63.6. The sense is that this was mostly felt in the retail sector due to the bounce in the construction sector as well as some of the health care readings. New credit applications slipped as well from 63.6 to 61.5—again something that may be related to a cautious approach in retail, which seems to be expecting a mediocre holiday season so far. Dollar collections improved a bit from 60.7 to 61.3. This is a consistent theme for the two sectors and reflects the better health of the overall customer base. There was also a gain in amount of credit extended from 65.9 to 66.8, a further reflection that customers may be in better shape than many had expected given the debacle at the start of the year. As is always the case, the next few months will be the most important as far as identifying trends in the retail community.

The index of unfavorable factors changed a little, improving from 52.1 to 52.3. Again, the individual factors showed more volatility. Of the factors that improved, rejections of credit applications stayed in the same range with its rise from 52.1 to 52.6, remaining stable, above 50. Accounts placed for collection improved by a larger margin, from 50.0 to 51.4. That is not a huge leap, but took it well into growth as opposed to hovering right on the brink of contraction. Disputes also improved from 50.2 to 50.9, and is trending in the right direction. Rounding out the improvements, filings for bankruptcies rose from 57.3 to 58.8 and was the best reading of them all. "The stress of the year has not yet caused a lot of business failure and it looks unlikely that this will be a problem going into the last half of the year," Kuehl said. "The most vulnerable businesses, as far as bankruptcy is concerned, are in retail and construction and it looks as if both will survive the year without many additional failures."

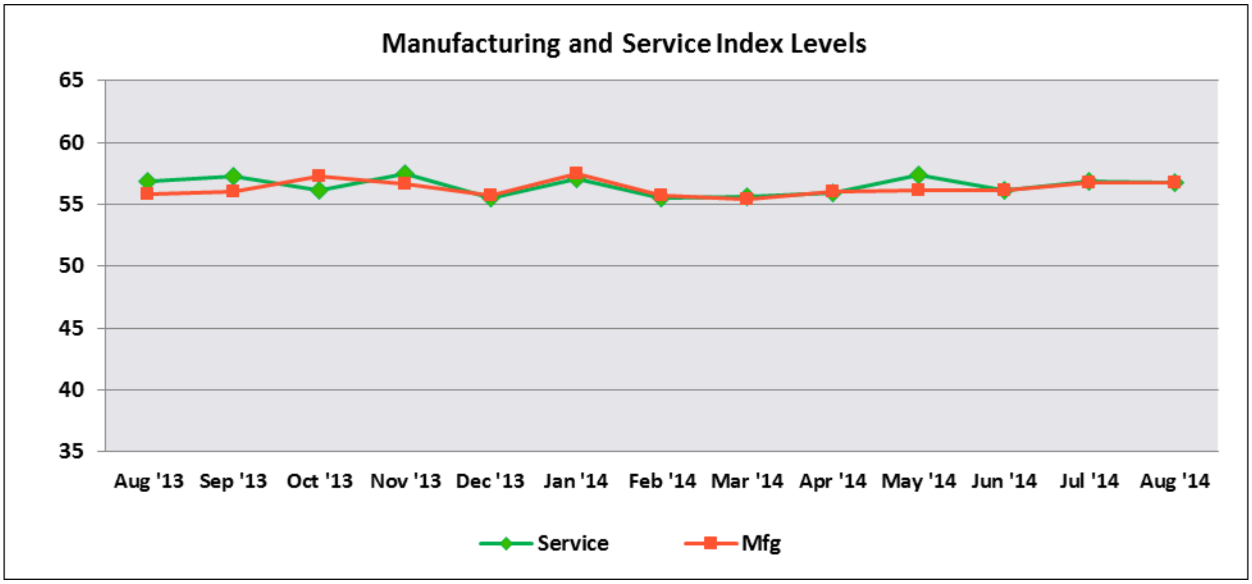
Deterioration appeared in dollar amount beyond terms, which fell into contraction territory, and dollar amount of customer deductions (52.0 to 51.4), which is not enough to create much concern. "The fall in dollar amount beyond terms from 51.2 to 48.9 is a concern given that this is its lowest point since June," Kuehl said. "Over the last year, this category has been hovering very close to the 50 expansion/contraction point and can't seem to get untracked."

Service Sector (seasonally adjusted)	Aug '13	Sep '13	Oct '13	Nov '13	Dec '13	Jan '14	Feb '14	Mar '14	Apr '14	May '14	Jun '14	Jul '14	Aug '14
Sales	63.9	63.8	60.6	63.4	55.7	63.4	60.9	59.6	61.9	66.6	62.1	65.6	63.6
New credit applications	59.1	59.2	58.1	59.1	56.7	57.0	58.5	58.5	59.8	60.7	61.3	63.6	61.5
Dollar collections	59.8	60.7	61.3	60.6	57.8	59.2	61.1	55.4	57.1	60.5	60.1	60.7	61.3
Amount of credit extended	64.5	63.4	62.8	64.5	63.6	64.4	62.3	64.5	63.1	65.7	64.3	65.9	66.8
Index of favorable factors	**61.8**	**61.8**	**60.7**	**61.9**	**58.4**	**61.0**	**60.7**	**59.5**	**60.5**	**63.4**	**61.9**	**63.9**	**63.3**
Rejections of credit applications	53.2	53.7	52.2	53.6	53.5	54.8	51.8	52.2	51.9	52.8	52.6	52.1	52.6
Accounts placed for collection	52.0	55.0	52.7	54.2	53.5	54.8	49.3	52.2	51.8	54.4	51.4	50.0	51.4
Disputes	53.3	52.6	51.4	52.8	51.3	53.3	52.2	51.2	52.1	50.8	50.4	50.2	50.9
Dollar amount beyond terms	49.7	51.5	50.9	54.5	49.3	52.3	50.6	52.0	50.5	50.4	48.9	51.2	48.9
Dollar amount of customer deductions	53.5	52.8	51.8	53.3	53.3	51.4	50.4	51.9	52.1	52.4	51.0	52.0	51.4
Filings for bankruptcies	59.6	60.1	60.3	59.4	60.4	60.5	58.4	58.4	59.2	59.8	59.0	57.3	58.8
Index of unfavorable factors	**53.6**	**54.3**	**53.2**	**54.6**	**53.6**	**54.5**	**52.1**	**53.0**	**53.0**	**53.4**	**52.2**	**52.1**	**52.3**
NACM Service CMI	**56.9**	**57.3**	**56.2**	**57.5**	**55.5**	**57.1**	**55.5**	**55.6**	**56.0**	**57.4**	**56.1**	**56.9**	**56.7**



August 2014 versus August 2013

"Compared to last August, performance improved significantly," Kuehl said. "Given that the trend over the last few months had been somewhat weaker than expected, this is good news."



Methodology Appendix

CMI data has been collected and tabulated monthly since February 2002. The index, published since January 2003, is based on a survey of approximately 1,000 trade credit managers in the second half of each month, with about equal representation between the manufacturing and service sectors. The survey asks respondents to comment whether they are seeing improvement, deterioration or no change for various favorable and unfavorable factors. There is representation from all states, except some of the less populated such as Vermont and Idaho.
The computation of seasonality is based on the formula used by the U.S. Census Bureau and most of the federal government's statistical gathering apparatus, making it possible to compare the CMI diffusion index with comparable indices, such as the PMI and other manufacturing and service sector indices.

Factors Making Up the Diffusion Index

As shown in the table below, 10 equally weighted items determine the index. These items are classified into two categories: favorable factors and unfavorable factors. A diffusion index is calculated for each item with the overall CMI being a simple average of the 10 items. Survey responses for each item capture the change—higher, lower or the same—in the current month compared to the previous month.

For positive indicators, the calculation is:

$$\frac{\text{Number of “higher” responses} + \tfrac{1}{2} \times \text{number of “same” responses}}{\text{Total number of responses}}$$

For negative indicators, the calculation is:

$$\frac{\text{Number of “lower” responses} + \tfrac{1}{2} \times \text{number of “same” responses}}{\text{Total number of responses}}$$

A resulting CMI number of more than 50 indicates an economy in expansion; less than 50 indicates contraction.

Favorable Factors	Why Favorable
Sales	Higher sales are considered more favorable than lower sales.
New credit applications	An increase in credit applications says that demand is greater this month, which represents increased business if credit is extended.
Dollar collections	Higher dollar collections represent improved cash flow for the selling firm and the ability of buying firms to pay.
Amount of credit extended	An increase for this item means business activity is expanding with greater sales via trade credit.
Unfavorable Factors*	**Why Unfavorable**
Rejections of credit applications	Increased rejections of credit applications means more marginal creditworthy customers are seeking trade credit and being denied.
Accounts placed for collection	As this item increases, the selling firm is having trouble collecting accounts, or conversely, there is an increase in buyers not paying.
Disputes	Higher dispute activity often is associated with cash flow problems of customers. They dispute the invoice to defer payment until later.
Dollar amount of receivables beyond terms	As this item becomes higher, it means customers are taking longer to pay.
Dollar amount of customer deductions	Higher deductions often are associated with cash flow problems of customers.
Filings for bankruptcies	Higher bankruptcy filings mean cash flow difficulties of customers are increasing.

**Note: When survey respondents report increases in unfavorable factors, the index numbers drop, reflecting worsening conditions.*

About the National Association of Credit Management

NACM, headquartered in Columbia, Maryland, supports more than 15,000 business credit and financial professionals worldwide with premier industry services, tools and information. NACM and its network of affiliated associations are the leading resource for credit and financial management information, education, products and services designed to improve the management of business credit and accounts receivable. NACM's collective voice has influenced our nation's policy makers on federal legislation concerning commercial business and trade credit for more than 100 years, and continues to play an active role in legislative issues that pertain to business credit and corporate bankruptcy. Its annual Credit Congress is the largest gathering of credit professionals in the world.

NACM has a wealth of member experts in the fields of business-to-business credit and law. Consider using NACM as a resource in the development of your next credit or finance story.

View CMI archives at http://web.nacm.org/cmi/cmi.asp.

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