



Report for December 2010

Issued December 30, 2010

National Association of Credit Management

Combined Sectors

The news for the end of the year was better than anticipated, matching the news coming from the retail sector in general. The gains in the overall CMI were impressive, but of more significance is the improvement in some key sub-sectors. For the past four to five months there were pretty steady gains in areas like sales and new credit applications—the sectors that usually herald some improvement in business conditions. But, until this month, the gains had not reached levels set earlier in the year. It now looks like there is some momentum heading into 2011; as the combined index now sits at 55.8.

Sales reached the highest point of the last 12 months, getting back to levels last seen in April when it was at 65.7. It now stands at 65.9, a solid improvement on the 61.9 registered in November. “The sales numbers have been rising in both manufacturing and service sectors and that is promising for the coming quarter,” said Chris Kuehl, PhD, NACM economic advisor and director of Armada Corporate Intelligence. “The improvement in new credit applications is more significant yet, given the impact it has on future growth. For the first time in well over three years, it broke 60. There is certainly reason for future optimism as this factor was only registering 54 to 54.8 as late as September. More and more businesses are now anticipating expansion and are seeking credit in order to meet that expected demand.”

The gains in credit extended and dollar collections were more modest, but both categories are now above 60 as well, pushing the favorable factor index to a relatively robust 62.1. The last time this occurred was back in March and April when there was a similar anticipation of growth in the overall economy.

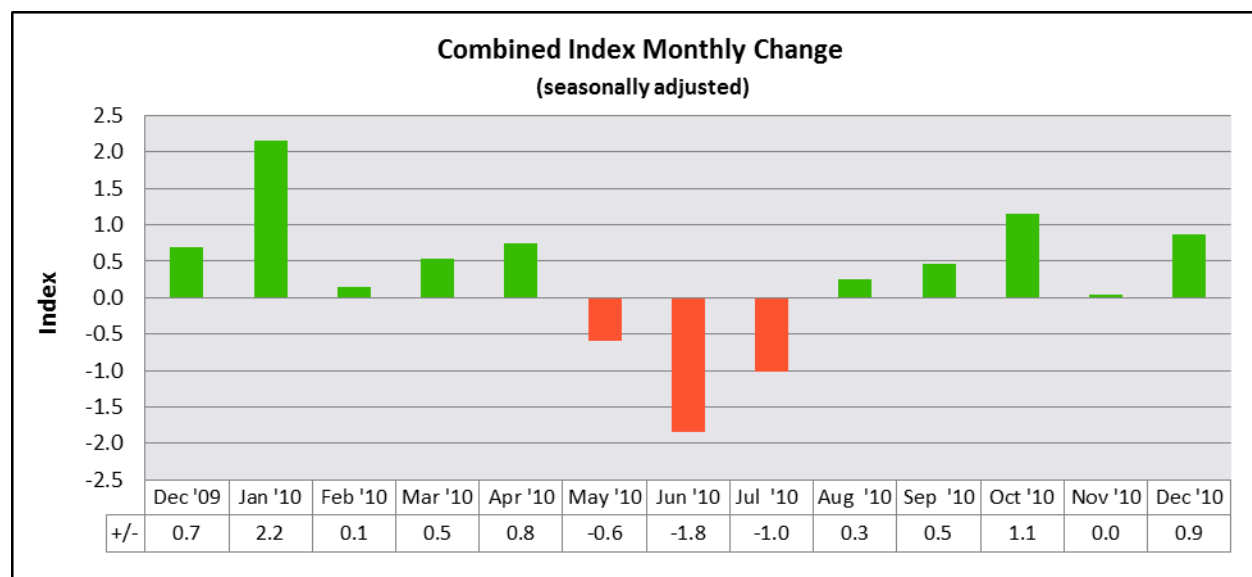
That is the good news. The not-so-good news is found in the index of unfavorable factors where there are trouble spots showing up. There were more rejections of credit applications, but some of that was expected with the overall increase in credit applications. The more troublesome aspect of these rejections indicates far more unqualified applicants than in the past. “This is the point in an economic recovery that provokes some desperation within the business community,” said Kuehl. “As key competitors start moving to capture more market share, their rivals have no choice but to try to keep pace, forcing companies to seek expansion regardless of whether they can really afford it.”

Several other unfavorable factors also showed weakness. There were more disputes, more accounts placed for collection and more filings for bankruptcy. The data suggest that another series of industry shakeouts are on the way. This is the period when weak companies that have been hanging on in anticipation of increased demand will either get the business boost they need to survive or will discover that the rescue is too late. Overall, the combined index of unfavorable factors remained steady compared to last month, but it’s expected that these numbers will worsen in the months to come—unless and until there is a more pronounced recovery in the economy.

The data support reports from the financial press in the last few months. A period of consolidation is likely in many industries as 2011 progresses. There are many companies that barely made it through the last year, hanging on for the opportunity to participate in the economic recovery. If that rebound is not manifested soon, they will not have the credit needed to survive and there will be a period of consolidation. There is already a great deal of action in the merger and acquisition world, mostly involving companies running out of options. “The CMI data show reason to be upbeat about the future, but there is also reason to be worried about some companies,” said Kuehl. “It has become a matter of winners and losers at this stage, as the competition focuses on who is positioned to gain in the next quarter or two.”

See page 5 of this report for information about the methodology and factors used to measure economic performance.

| Combined Manufacturing and Service Sectors (seasonally adjusted) | Dec '09 | Jan '10 | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec '10 |
|---|----------------|----------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|----------------|
| Sales | 56.7 | 60.7 | 60.9 | 65.0 | 65.7 | 64.5 | 59.0 | 57.2 | 57.6 | 58.6 | 60.8 | 61.9 | 65.9 |
| New credit applications | 54.2 | 57.0 | 57.7 | 57.5 | 57.4 | 58.6 | 57.4 | 54.1 | 54.6 | 54.8 | 56.8 | 58.2 | 60.1 |
| Dollar collections | 58.0 | 61.3 | 61.1 | 61.9 | 62.1 | 59.7 | 59.4 | 56.3 | 57.7 | 60.0 | 61.9 | 58.6 | 60.7 |
| Amount of credit extended | 55.2 | 58.8 | 59.4 | 61.3 | 61.3 | 60.2 | 55.9 | 56.0 | 57.1 | 58.7 | 59.8 | 61.2 | 61.7 |
| Index of favorable factors | 56.0 | 59.4 | 59.8 | 61.4 | 61.6 | 60.7 | 57.9 | 55.9 | 56.7 | 58.0 | 59.8 | 60.0 | 62.1 |
| Rejections of credit applications | 50.1 | 51.4 | 51.0 | 50.1 | 50.9 | 50.7 | 51.0 | 52.0 | 50.7 | 49.1 | 51.4 | 51.0 | 50.8 |
| Accounts placed for collection | 50.9 | 50.7 | 50.4 | 51.1 | 50.6 | 54.5 | 51.4 | 49.3 | 51.1 | 50.4 | 51.7 | 52.5 | 51.5 |
| Disputes | 51.0 | 51.4 | 52.2 | 52.2 | 51.7 | 51.3 | 50.4 | 50.6 | 50.9 | 50.8 | 49.9 | 50.8 | 49.2 |
| Dollar amount beyond terms | 51.4 | 52.2 | 52.0 | 51.5 | 51.9 | 50.2 | 49.1 | 49.4 | 47.0 | 49.1 | 50.9 | 48.9 | 53.4 |
| Dollar amount of customer deductions | 51.3 | 52.5 | 51.2 | 51.7 | 55.7 | 51.8 | 50.3 | 50.5 | 49.6 | 50.6 | 48.9 | 50.2 | 49.6 |
| Filings for bankruptcies | 50.5 | 54.7 | 56.3 | 55.3 | 57.6 | 57.6 | 56.6 | 55.0 | 56.9 | 55.7 | 57.0 | 56.3 | 55.4 |
| Index of unfavorable factors | 50.8 | 52.2 | 52.2 | 52.0 | 53.1 | 52.7 | 51.5 | 51.1 | 51.0 | 50.9 | 51.6 | 51.6 | 51.7 |
| NACM Combined CMI | 52.9 | 55.1 | 55.2 | 55.7 | 56.5 | 55.9 | 54.1 | 53.0 | 53.3 | 53.8 | 54.9 | 55.0 | 55.8 |



Manufacturing Sector

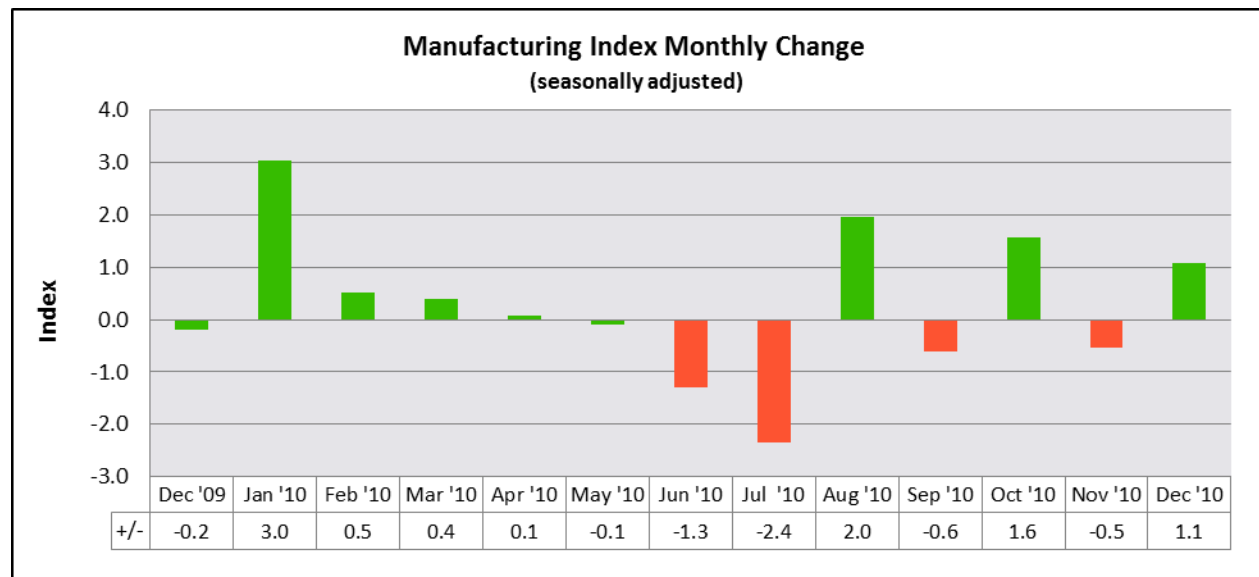
The manufacturing sector continues to surprise most analysts. The expectation has been that, at some point, all that manufacturing productivity would grind to a halt as the various factors driving it thus far started to fade. There was the drive to build up inventory after most operations had allowed their stockpiles to erode, which carried the sector through the end of 2009. In 2010, the anticipation of more economic growth drove activity through the spring, but the economy slumped again when that growth didn't appear. Then, with a stronger-than-expected consumer response at the end of the year, there was another potential boost to manufacturing and that seems to be reflected in December's sales and new credit applications data. Sales numbers now look better than they have since March's 66.9, and the new credit applications number is better than it has been in over two years. There has been a smaller boost in the amount of credit extended, moving from 61.2 to 61.6, but the real point is that this number is above 60.

Overall, the favorable factors showed a solid gain, moving from 59.8 to 61.9, the highest point since the March reading of 62.1. The news on unfavorable factors wasn't quite as uplifting, but did see more progress than those of the service sector. The manufacturing index moved from 54.7 to 55.8, gaining over a full point, taking this number back to what was reported in April and May.

The movement in unfavorable factors was minor from November to December, with a couple of notable exceptions. Dollars beyond terms improved quite a bit over the reporting period, moving from 49.4 to 53.9. This was the only category to see much movement and there are some suggestions as to why this might be the case. A number of comments suggested companies had become far more aggressive in collecting on receivables, especially as year-end approached, which apparently had an impact on the level of dollar exposure. There was also a slight increase in the number of rejected credit applications and the number of accounts placed for collection as more companies struggle to stay in the game. If the past is prologue, there will be an acceleration of these troubled businesses followed by marked improvements in unfavorable factors as the survivors expand their market share in the wake of absent competitors.

For the past few months, the manufacturing index has been unusually volatile—up in August, October and December, while falling in September and November. The reasons for this erratic behavior are varied, but much of it stems from the fact that manufacturing has been largely reactive for the past year. Periods of anticipated growth propelled manufacturers to gear up, and when that promise of expansion faded, retreat followed. This latest surge may be related to the stronger consumer numbers over the holiday season and now the question is whether this is sustainable.

| Manufacturing Sector <i>(seasonally adjusted)</i> | Dec '09 | Jan '10 | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec '10 |
|---|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Sales | 55.8 | 61.8 | 62.5 | 66.9 | 65.2 | 66.0 | 59.1 | 56.1 | 59.4 | 57.9 | 59.3 | 62.2 | 66.6 |
| New credit applications | 55.2 | 54.0 | 57.8 | 57.9 | 57.1 | 58.9 | 58.9 | 53.7 | 54.3 | 54.4 | 54.9 | 57.8 | 59.1 |
| Dollar collections | 56.0 | 61.5 | 59.6 | 61.4 | 60.9 | 59.7 | 59.0 | 53.0 | 60.1 | 61.1 | 61.0 | 57.9 | 60.5 |
| Amount of credit extended | 55.2 | 59.2 | 60.7 | 62.0 | 62.1 | 58.9 | 58.2 | 55.8 | 56.0 | 57.3 | 59.9 | 61.2 | 61.6 |
| Index of favorable factors | 55.6 | 59.1 | 60.2 | 62.1 | 61.3 | 60.9 | 58.8 | 54.6 | 57.5 | 57.7 | 58.8 | 59.8 | 61.9 |
| Rejections of credit applications | 49.5 | 52.4 | 51.4 | 50.9 | 52.3 | 51.6 | 51.8 | 52.0 | 52.6 | 49.6 | 53.2 | 52.1 | 51.3 |
| Accounts placed for collection | 51.0 | 51.3 | 51.0 | 51.9 | 52.0 | 54.3 | 54.3 | 48.5 | 52.8 | 51.9 | 53.6 | 52.7 | 51.1 |
| Disputes | 50.1 | 50.7 | 51.9 | 51.5 | 51.8 | 50.0 | 50.6 | 50.8 | 51.3 | 50.0 | 49.5 | 48.6 | 48.1 |
| Dollar amount beyond terms | 51.4 | 52.5 | 53.3 | 51.3 | 52.2 | 50.1 | 50.3 | 50.4 | 51.0 | 49.6 | 55.2 | 49.4 | 53.9 |
| Dollar amount of customer deductions | 49.8 | 52.2 | 51.3 | 51.6 | 50.8 | 51.0 | 49.2 | 49.9 | 48.4 | 49.4 | 48.5 | 48.8 | 49.4 |
| Filings for bankruptcies | 46.6 | 55.4 | 56.5 | 54.8 | 56.6 | 59.5 | 55.6 | 53.4 | 57.1 | 55.8 | 57.7 | 56.7 | 56.5 |
| Index of unfavorable factors | 49.7 | 52.4 | 52.6 | 52.0 | 52.6 | 52.7 | 52.0 | 50.8 | 52.2 | 51.1 | 52.9 | 51.4 | 51.7 |
| NACM Manufacturing CMI | 52.1 | 55.1 | 55.6 | 56.0 | 56.1 | 56.0 | 54.7 | 52.4 | 54.3 | 53.7 | 55.3 | 54.7 | 55.8 |



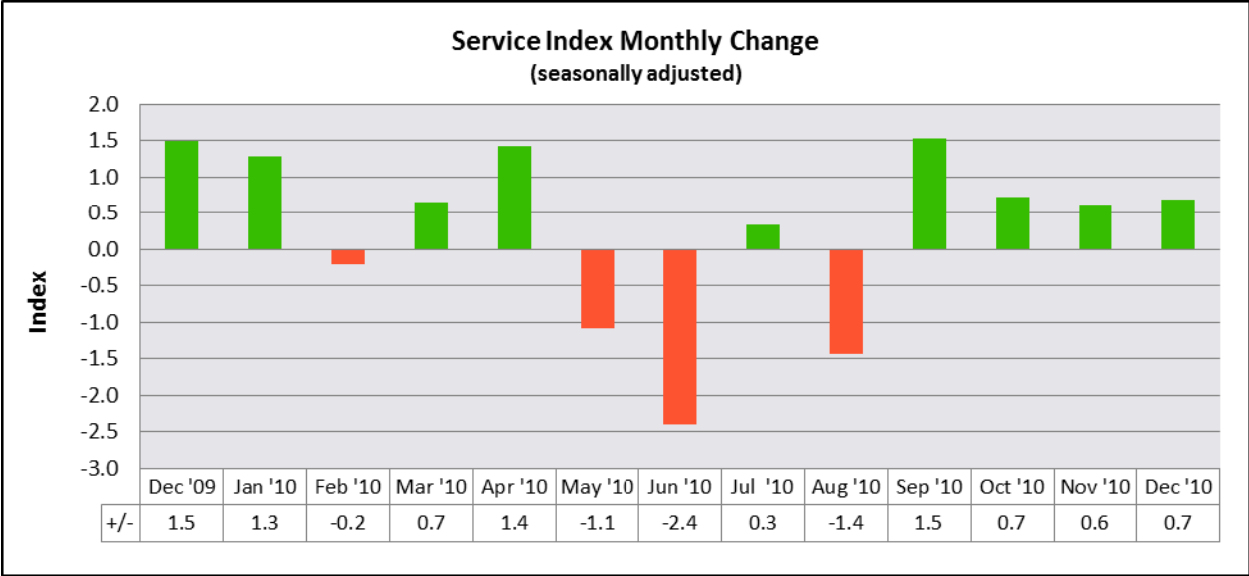
Service Sector

Service sector performance was essentially flat, but this sector has been far less volatile than the manufacturing sector. The numbers for the service index have been steady and positive, inching up slowly month by month from November's 55.2 to December's 55.8. The index is now standing higher than it has in over two years. The increase in sales was not quite as dramatic as manufacturing's, but was still responsive—up to 65.1 from 61.6—putting it close to April levels. The number of new credit applications jumped a bit as well, from 58.6 to 61.1. Overall, the favorable factors moved from 60.2 to 62.2, exceeding the level reached in April 2010.

Much of what has pushed this sector is in retail and the core service areas like transportation and professional services. Financial services continue to struggle and there is still very little sign of life in the construction arena. The bad news is that there are more problems with the unfavorable factors. Again, there is little that is highly dramatic, but most of the categories are in decline: rejections of credit applications, accounts placed for collection, disputes and dollar amount of customer deductions. The exception is with dollar amounts beyond terms. Here again there seems to be a connection to the effort to collect and keep debts under control.

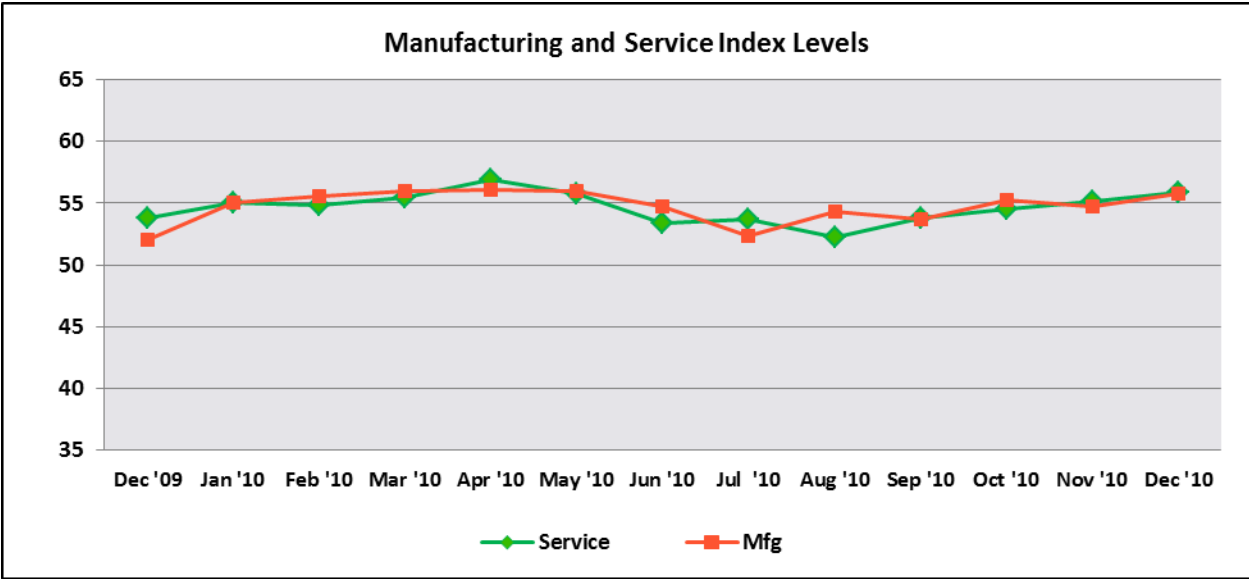
The service sector is a very diverse collection of business categories and that can sometimes obscure the details for specific categories. Some of the good and bad categories have been discussed above, but there are others that merit attention. There is a consistent level of growth in health care-related industries and there are some new signs of life with the transportation sector (especially airlines). Going forward, there will be a great deal of attention paid to retail to see if the consumer is really starting to emerge.

| Service Sector (seasonally adjusted) | Dec '09 | Jan '10 | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec '10 |
|---|----------------|----------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|----------------|
| Sales | 57.5 | 59.6 | 59.3 | 63.0 | 66.3 | 63.0 | 58.8 | 58.2 | 55.7 | 59.3 | 62.2 | 61.6 | 65.1 |
| New credit applications | 53.2 | 60.1 | 57.6 | 57.1 | 57.7 | 58.2 | 55.9 | 54.5 | 54.8 | 55.1 | 58.7 | 58.6 | 61.1 |
| Dollar collections | 59.9 | 61.2 | 62.7 | 62.4 | 63.2 | 59.7 | 59.7 | 59.7 | 55.2 | 59.0 | 62.9 | 59.2 | 60.9 |
| Amount of credit extended | 55.2 | 58.3 | 58.2 | 60.5 | 60.5 | 61.5 | 53.7 | 56.3 | 58.1 | 60.0 | 59.6 | 61.2 | 61.8 |
| Index of favorable factors | 56.5 | 59.8 | 59.4 | 60.8 | 62.0 | 60.6 | 57.0 | 57.2 | 56.0 | 58.4 | 60.9 | 60.2 | 62.2 |
| Rejections of credit applications | 50.6 | 50.4 | 50.6 | 49.4 | 49.6 | 49.7 | 50.3 | 51.9 | 48.7 | 48.7 | 49.6 | 49.8 | 50.3 |
| Accounts placed for collection | 50.7 | 50.1 | 49.9 | 50.2 | 49.2 | 54.8 | 48.5 | 50.1 | 49.4 | 48.9 | 49.9 | 52.4 | 52.0 |
| Disputes | 51.9 | 52.1 | 52.5 | 52.9 | 51.6 | 52.7 | 50.3 | 50.5 | 50.5 | 51.5 | 50.3 | 52.9 | 50.3 |
| Dollar amount beyond terms | 51.4 | 51.9 | 50.6 | 51.6 | 51.7 | 50.3 | 47.9 | 48.4 | 43.1 | 48.5 | 46.6 | 48.5 | 52.9 |
| Dollar amount of customer deductions | 52.7 | 52.9 | 51.1 | 51.8 | 60.5 | 52.6 | 51.4 | 51.0 | 50.8 | 51.7 | 49.4 | 51.6 | 49.9 |
| Filings for bankruptcies | 54.3 | 53.9 | 56.0 | 55.8 | 58.6 | 55.7 | 57.6 | 56.6 | 56.6 | 55.5 | 56.3 | 55.9 | 54.3 |
| Index of unfavorable factors | 52.0 | 51.9 | 51.8 | 52.0 | 53.5 | 52.6 | 51.0 | 51.4 | 49.8 | 50.8 | 50.4 | 51.8 | 51.6 |
| NACM Service CMI | 53.8 | 55.0 | 54.8 | 55.5 | 56.9 | 55.8 | 53.4 | 53.7 | 52.3 | 53.8 | 54.6 | 55.2 | 55.8 |



December 2010 vs. December 2009

The story of the last year appears to be consistency. For 12 months now, the CMI has wavered in a very narrow range between 52 and 56. That is nothing to prompt dancing in the streets, but it also suggests that the recovery has been solid, albeit slow. The other interesting point is that for the last couple of months, the two sectors have been tracking in tandem and that is generally a good signal for the economy as a whole.



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 on 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 those from the Purchasing Managers, the Supply Chain Managers and others.

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:

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

For negative indicators, the calculation is:

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

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

The National Association of Credit Management (NACM), headquartered in Columbia, Maryland, supports approximately 18,000 business credit and financial professionals worldwide with premier industry services, tools and information. NACM and its network of

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