



Report for January 2010

Issued February 1, 2010

National Association of Credit Management

Combined Sectors

The latest data are starting to turn in a decidedly positive direction; GDP numbers are the best in over a year and a half, suggesting that the recession is in clear retreat. After a mild recovery in the third quarter, numbers jumped 5.8% in the fourth. The bulk of this growth is attributed to manufacturers starting to replenish inventories, mostly since the beginning of December. This shift in strategy is reflected in the Credit Managers' Index (CMI) numbers as well. "The jump in manufacturing was stark and unexpected and, since the decline registered in the last iteration of the index, there has been a major leap in some critical areas," said Chris Kuehl, Ph.D., NACM economist. "The combined CMI saw a jump from 52.9 to 55.1, which is impressive enough, but the real movement came from the manufacturing side," he said. Reinforcing the message coming from the economy as a whole, the manufacturing sector jumped from 52.1 to 55.1, reversing the trend from the December index when the sector stagnated and slipped in terms of positive factors.

There was an improved atmosphere in both manufacturing and service sectors with the most activity in the combined index's favorable factors, specifically sales and new credit applications. Sales in the combined index jumped from 56.7 to 60.7, marking the first time this figure has been above 60 in 18 months. There was also progress in new credit applications—a jump from 54.2 to 57—signaling movement in the credit sector despite ongoing issues in the financial community. One of the biggest leaps came from dollar collections, which sported readings in the 40s just nine months ago and is now at 61.3. The same pattern was seen in amount of credit extended, now standing at 58.8 after sitting in the 40s just five months ago.

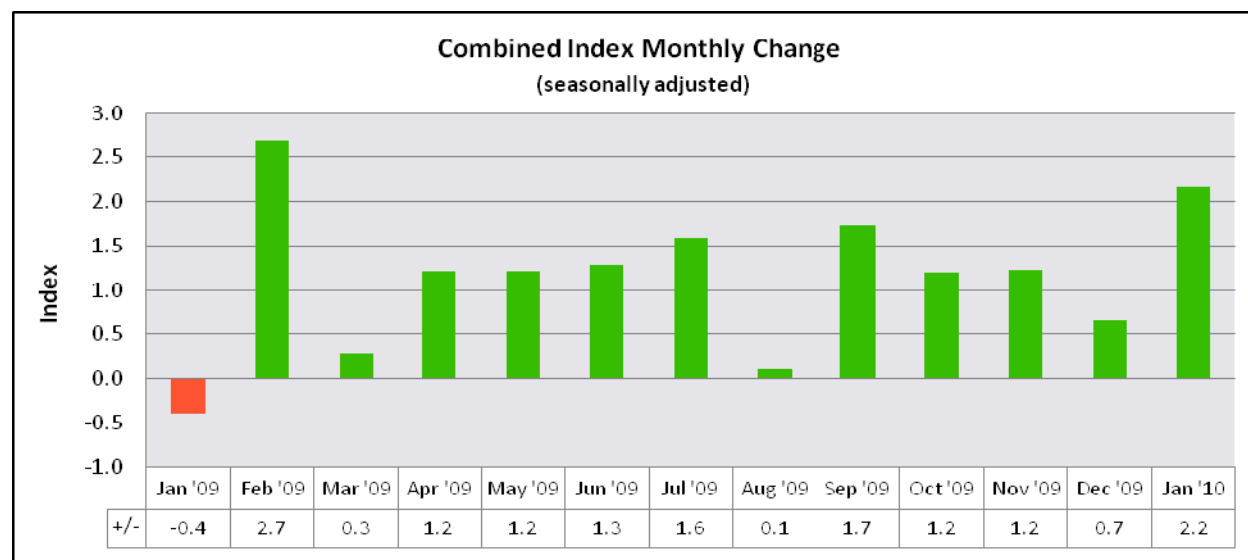
"The past pattern in the index suggests that this is developing into a classic recession exit," said Kuehl. "The deterioration of inventory and the dramatic reduction in capacity utilization meant that any spark of demand would propel business out of this predicament and, as in past recessions, the months following the end of these strategies would show substantial growth. The trillion-dollar question is whether this growth surge can be maintained throughout the rest of the year."

Thus far, these are the highest numbers seen in the index since February 2009 when the initial impetus of the recession was broken. Since then, growth has been even, but not dramatic. That trend of slow growth is likely to return, but the suggestion from this month's data is that there will be pretty substantial gains for the bulk of the first quarter.

The service sector was not as dramatic as the manufacturing sector, but there was growth. The same factors seemed to be at work—increased sales and expanded availability of money. In both sectors there has been some improvement in terms of the number of accounts placed for collection and the number of disputes, and there has been a fairly steady decline in the number of bankruptcies as well. All in all, the CMI numbers of the last few months signal that business is attempting to catch up and position itself for the growth that has now finally arrived.

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)	Jan '09	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10
Sales	29.5	34.1	35.2	37.4	41.8	44.8	48.6	48.4	49.9	51.1	55.0	56.7	60.7
New credit applications	42.7	44.9	44.3	47.8	48.2	50.7	52.6	49.3	50.0	52.7	55.4	54.2	57.0
Dollar collections	47.5	47.1	48.4	48.0	48.8	51.2	50.8	50.5	53.4	54.7	55.8	58.0	61.3
Amount of credit extended	40.5	42.2	41.8	42.3	44.3	46.1	48.2	48.0	49.3	53.6	54.6	55.2	58.8
Index of favorable factors	40.0	42.1	42.4	43.9	45.8	48.2	50.0	49.1	50.6	53.0	55.2	56.0	59.4
Rejections of credit applications	45.9	46.7	47.8	47.4	47.4	47.9	47.5	49.0	48.4	49.0	49.3	50.1	51.4
Accounts placed for collection	36.8	37.8	37.1	38.5	40.2	40.5	44.0	43.6	45.3	47.1	49.5	50.9	50.7
Disputes	43.4	44.8	44.1	47.2	47.5	47.7	50.2	49.7	50.8	51.0	49.6	51.0	51.4
Dollar amount beyond terms	30.6	42.0	42.3	40.5	43.4	43.6	45.3	46.2	48.1	48.1	49.0	51.4	52.2
Dollar amount of customer deductions	45.2	46.2	45.5	49.8	47.5	48.9	49.2	50.6	51.8	50.5	51.3	51.3	52.5
Filings for bankruptcies	35.4	38.4	40.5	40.2	42.3	42.8	43.7	45.8	51.5	52.6	53.0	50.5	54.7
Index of unfavorable factors	39.5	42.6	42.9	43.9	44.7	45.2	46.7	47.5	49.3	49.7	50.3	50.8	52.2
NACM Combined CMI	39.7	42.4	42.7	43.9	45.1	46.4	48.0	48.1	49.8	51.0	52.3	52.9	55.1



Manufacturing Sector

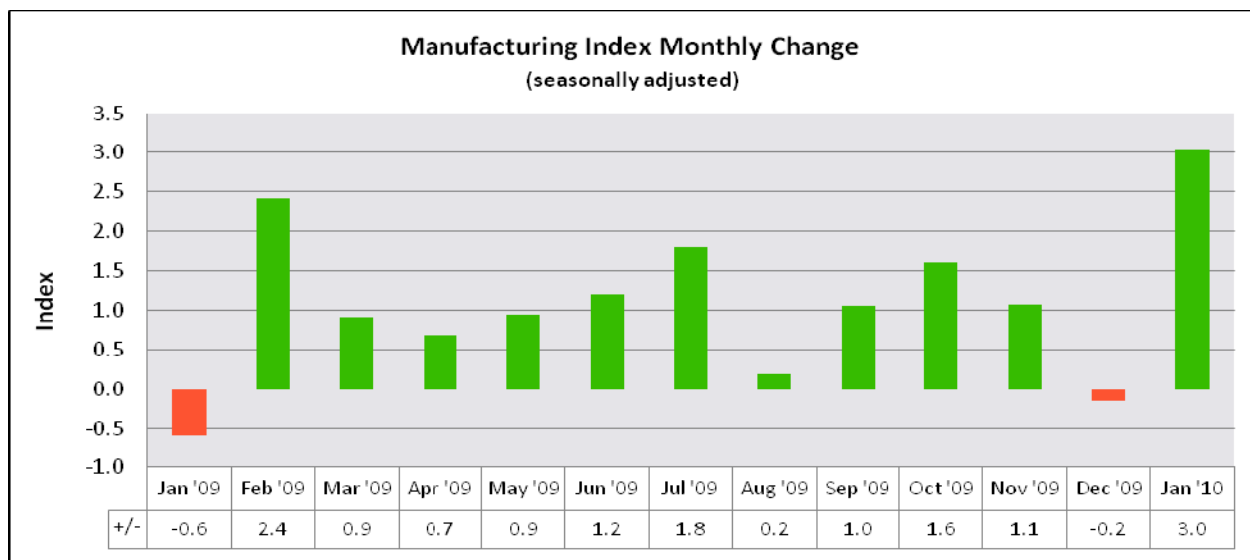
A pattern appears each time there is a recession and, in this downturn, that pattern has been as visible as it was during the recessions of the early 1970s and 1980s. The strategy employed by most companies in the face of financial strain is to reduce costs to the barest of minimums, which involves slashing the workforce, postponing or eliminating capital expenditures and reducing inventory to the lowest possible level. The CMI's figures on capacity utilization reflect this strategy as they have fallen to levels not seen since the depths of the 1980s double-dip recession. The strategy for retailers was as extreme as it has ever been—betting that the consumer would grab whatever they could find during the holiday season—and the effort seemed to work, as the retailers managed to pull off a decent December in spite of the limited offerings. On the manufacturing side, this inventory reduction was extreme and extended, such that by the end of the year supply was dangerously low, especially if one wanted to hang onto market share when recovery arrived.

“For two months, the CMI told a story. The number of disputes fell, dollars out for collection declined and so did almost all the factors that indicated debt was going unpaid,” said Kuehl. He further commented that the process of catching up on that debt was the first step toward returning inventory levels, and companies that needed to buy raw materials for production had to get current with their creditors, a process that began in earnest in November and in some cases as early as October. By December, the purchasing had officially started. The evidence of this

recovery was noticeable in other sectors as well. The first transportation sector that would see gains when factories started back up was rail and, sure enough, freight volumes started to climb in the rail sector in November and have been climbing steadily ever since.

It is far too early to assert that manufacturing has finally escaped the ravages of this recession, but the first stage is underway. The boost provided by the need to replenish inventory has already helped to stabilize some of the metals prices and has resulted in renewed activity in everything from transportation to warehousing. The next step in the recovery will be for consumer demand to draw down this newly-established inventory and necessitate its replacement. This has yet to develop, but there are some hopeful signs. For the moment, the good news lies in the future, reflected in the manufacturing index by jumps in sales as well as amount of credit extended.

Manufacturing Sector <i>(seasonally adjusted)</i>	Jan '09	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10
Sales	31.6	34.7	36.7	39.6	40.7	45.4	48.7	48.4	48.7	52.0	56.3	55.8	61.8
New credit applications	44.8	45.2	44.6	50.7	49.3	51.1	55.3	48.6	50.5	52.9	56.8	55.2	54.0
Dollar collections	48.2	48.3	49.5	48.0	47.5	51.6	51.7	51.3	52.1	55.7	53.1	56.0	61.5
Amount of credit extended	39.6	40.5	41.8	44.1	44.2	45.8	49.3	48.9	48.8	53.5	53.4	55.2	59.2
Index of favorable factors	41.1	42.2	43.1	45.6	45.4	48.5	51.3	49.3	50.0	53.5	54.9	55.6	59.1
Rejections of credit applications	46.0	46.5	48.1	47.2	47.4	47.8	47.5	50.6	48.9	49.6	49.5	49.5	52.4
Accounts placed for collection	39.1	38.1	37.7	38.6	41.8	41.2	44.1	43.3	46.3	47.1	49.5	51.0	51.3
Disputes	42.6	44.4	44.4	45.8	47.6	46.1	49.3	48.2	49.5	50.9	48.0	50.1	50.7
Dollar amount beyond terms	30.8	46.5	48.1	42.8	44.5	45.3	46.3	48.1	48.3	47.9	50.0	51.4	52.5
Dollar amount of customer deductions	44.6	44.5	45.6	47.6	46.6	47.6	47.8	50.4	50.8	49.9	50.3	49.8	52.2
Filings for bankruptcies	36.4	39.2	40.6	39.6	43.6	43.2	43.1	47.3	51.7	52.1	55.4	46.6	55.4
Index of unfavorable factors	39.9	43.2	44.1	43.6	45.2	45.2	46.4	48.0	49.2	49.6	50.4	49.7	52.4
NACM Manufacturing CMI	40.4	42.8	43.7	44.4	45.3	46.5	48.3	48.5	49.6	51.2	52.2	52.1	55.1



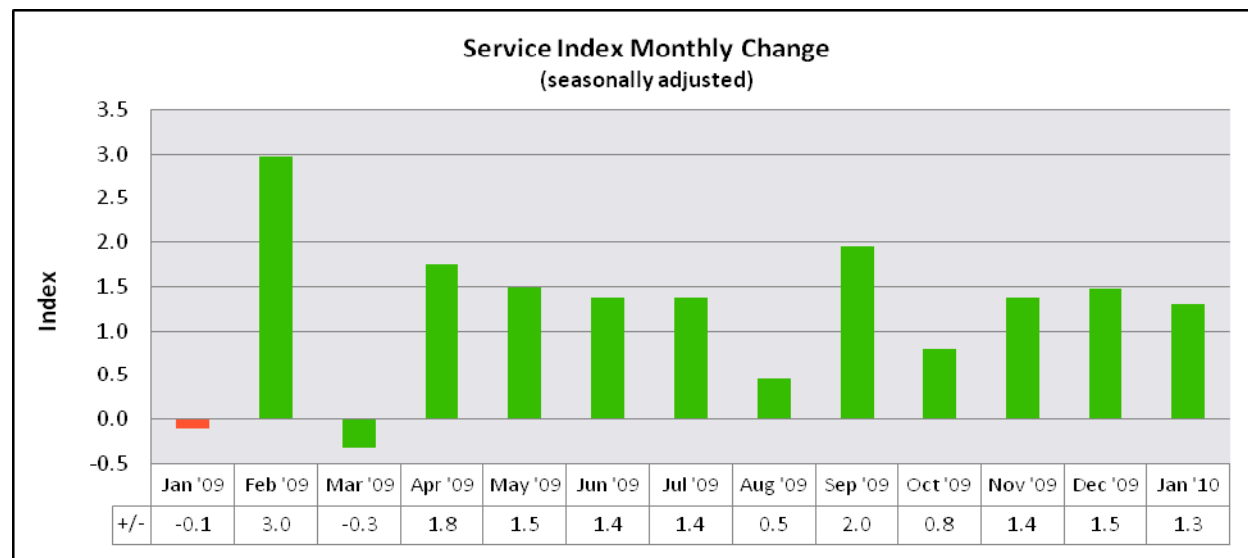
Service Sector

There was less dramatic movement in the service sector, but progress was registered nonetheless. The increase in sales was notable, although not as significant as in manufacturing this month. What is good to see is the index has crested above 60 in both new credit applications and dollar collections. Kuehl noted that it was only four or five months ago that both of these factors had readings in the 40s and, a year ago, new credit applications was in the 30s. The credit squeeze has certainly not ended, but there is more available now than there has been for almost 18

months. The system has not returned to the profligate ways of the last decade, but that is likely a good thing. The old-school thinking that used to dominate the banks and financial institutions seems to have made a bit of a comeback, which is now freeing up credit for those that are traditionally creditworthy.

“Unfortunately, the most noteworthy aspect of the service numbers was that the negative factors did not shrink as much as hoped, with the combined index of unfavorable factors only dropping from 52 to 51.9—a very small decline, and not the strong positive trend seen in manufacturing,” said Kuehl. The prime reason for this slowdown seems to be more accounts placed for collection than last month, attributable to the fact that many retail operations did not manage to escape the Christmas season unscathed. This pattern occurs every year as the holiday shopping season is make-or-break for retail and there are always casualties of consumer tastes and preferences. Still, more retailers went into this year’s season weaker than in the past and some did not make it, and these troubled accounts will likely add to the number of bankruptcies in months to come.

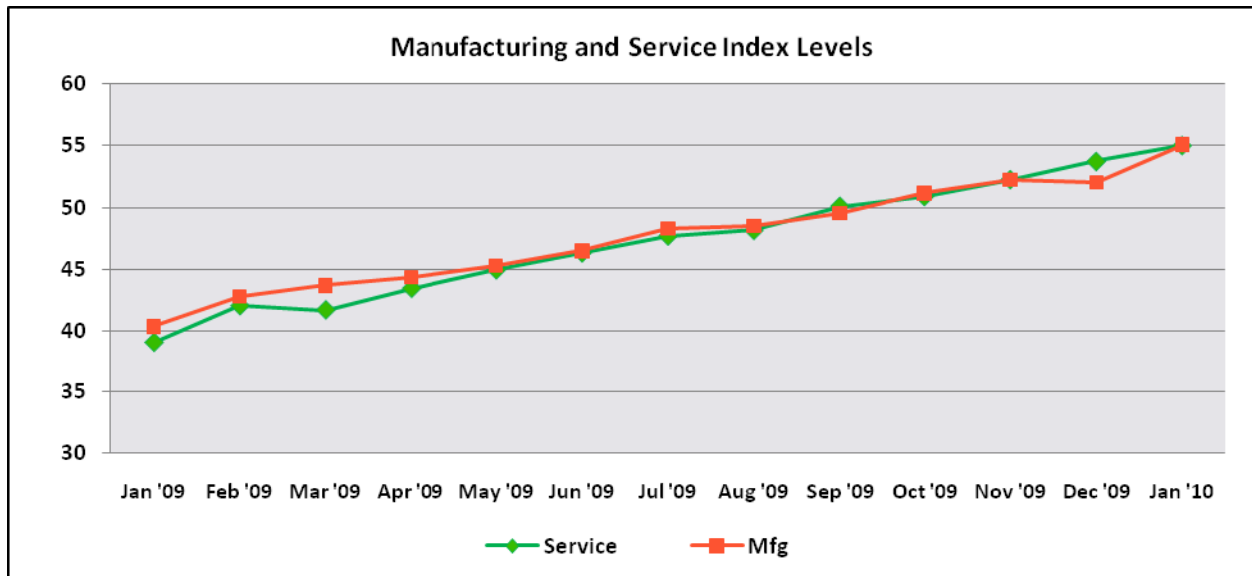
Service Sector (seasonally adjusted)	Jan '09	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10
Sales	27.3	33.5	33.7	35.2	42.9	44.1	48.4	46.5	51.0	50.3	53.7	57.5	59.6
New credit applications	40.5	44.6	44.0	44.9	47.2	50.3	49.9	49.5	49.5	52.4	54.1	53.2	60.1
Dollar collections	46.8	45.9	47.4	48.0	50.0	50.8	49.8	50.5	54.8	53.7	58.6	59.9	61.2
Amount of credit extended	41.4	43.9	41.8	40.6	44.3	46.4	47.1	46.3	49.8	53.8	55.7	55.2	58.3
Index of favorable factors	39.0	41.9	41.7	42.2	46.1	47.9	48.8	48.2	51.2	52.5	55.5	56.5	59.8
Rejections of credit applications	45.7	46.9	47.5	47.7	47.4	48.1	47.4	48.5	47.9	48.5	49.2	50.6	50.4
Accounts placed for collection	34.4	37.5	36.5	38.5	38.7	39.8	43.9	43.7	44.3	47.1	49.4	50.7	50.1
Disputes	44.1	45.2	43.9	48.6	47.3	49.4	51.2	49.0	52.1	51.0	51.2	51.9	52.1
Dollar amount beyond terms	30.3	37.4	36.6	38.3	42.3	41.9	44.3	49.5	47.9	48.3	48.0	51.4	51.9
Dollar amount of customer deductions	45.7	48.0	45.4	52.0	48.4	50.2	50.7	51.1	52.7	51.1	52.3	52.7	52.9
Filings for bankruptcies	34.4	37.7	40.4	40.8	41.0	42.3	44.4	47.0	51.3	53.0	50.7	54.3	53.9
Index of unfavorable factors	39.1	42.1	41.7	44.3	44.2	45.3	47.0	48.1	49.4	49.8	50.1	52.0	51.9
NACM Service CMI	39.1	42.0	41.7	43.5	45.0	46.3	47.7	48.2	50.1	50.9	52.3	53.8	55.0



January 2010 vs. January 2009

The contrast between January 2009 and January 2010 is stark and the distance between the two is likely as broad as it will be for some time. It was a year ago that the recession reached its deepest point and the index showed

numbers buried in the 40s. Now the index has climbed into solid expansion territory and is well into the mid 50s. It is not likely that this trajectory will be maintained indefinitely as there are still questions about how fast consumers will start to draw down new inventory, but there is also not much that would suggest a major decline at this point.



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 1000 trade credit managers during the last 10 days of the 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 or 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.*



National Association of Credit Management

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 Affiliated Associations are the leading resource for credit and financial management information and education, delivering products and services, which improve the management of business credit and accounts receivable. NACM's collective voice has influenced legislative results concerning commercial business and trade credit to our nation's policy makers for more than 100 years, and continues to play an active part in legislative issues pertaining to business credit and corporate bankruptcy.

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