Report for July 2011

Issued July 29, 2011

National Association of Credit Management

Combined Sectors

The best that can be said about this month's Credit Managers' Index (CMI) is that things did not get appreciably worse. The latest data suggest a third month of slump, and it appears the economy is languishing in a state that is not quite in crisis but which isn't showing energy either. For the third month in a row, the overall index was slightly over 54. The fact that it went up by .4 is nothing much to cheer, as the overall index had been over 55 for the six months prior to May's slip. "If there is anything to be somewhat encouraged by it is that manufacturing improved over the really down month last July, but at the same time there was weakness in the service sector that didn't appear the previous month," said Chris Kuehl, PhD, managing director of Armada Corporate Intelligence and economic advisor to the National Association of Credit Management (NACM).

Very little changed as far as favorable factors were concerned. Sales were essentially flat at 60—slightly down from 60.8—but that is a pretty solid sign given the declines noted in other areas. "It appears sales numbers have started to stabilize and are not that far from the highs reached a few months ago when they crested at 66.3," said Kuehl. The biggest decline was in dollar collections—from 58.1 to 56.2. There have been other signs that collection activity has been slowing, which is consistent with the overall assessments of the economy of late.

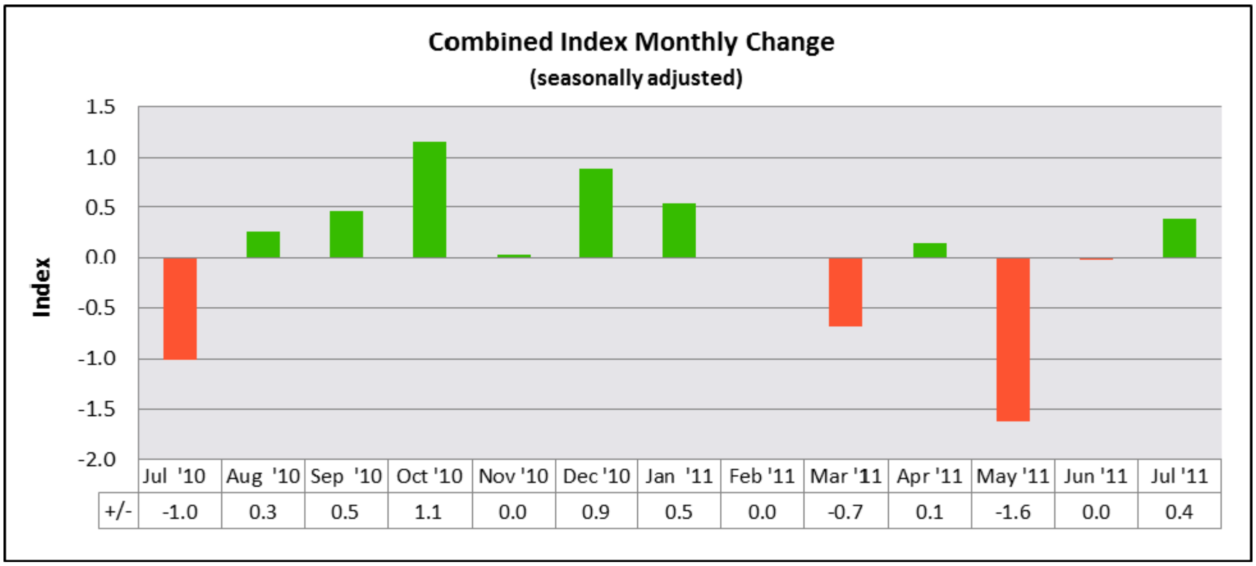
"In comparing the CMI readings to other indices, it is apparent the economy has still not committed to either continued growth or a real decline," said Kuehl. "There have been some positive signs from the latest set of leading economic indicators released from the Conference Board, but there have also been renewed signs of distress as far as consumer confidence is concerned. Not surprisingly there is a sense that much has stalled in the economy as uncertainty has been the rule of the day."

Unfavorable factors don't show signs of increased stress and there isn't a lot to suggest much panic—at least not yet. There was a pretty solid improvement—from 50 to 55.6—in the dollar amount of customer deductions. This was accompanied by modest improvements in the number of rejected credit applications, which improved from 50.9 to 51. There was also improvement in the number of disputes, from 49.3 to 50. "These are not major shifts by any stretch of the imagination, but at least they are not trending downward any further," said Kuehl.

The overall index barely changed and the manufacturing and service sectors have simply swapped positions again as far as stress is concerned. The CMI numbers for the last three months show a general slowdown in business activity. There has been a slump in sales, a reduction in the number of new credit applications and a slowdown in the collection process. The economy is essentially stalled and the question is whether this is a reaction to something short term or a reflection of some greater underlying trend. The CMI data hint that the situation is temporary and related to uncertain factors gripping the economy. Much of this information is more anecdotal than anything that can be pinned onto hard data. The majority of the information from the banking sector suggests there is money to borrow. There is available trade credit according to most sources. Businesses are sitting on more cash than they have in a long time and most companies are not having issues paying their bills. The problem is that almost everybody is worried about contingency plans and are sitting back as they wait for something to change.

The demand needed is not there yet and nobody is quite sure why. The jobless situation is certainly a worry, but the fact is that 91% of the workforce is employed. They are nervous about spending and as long as they stay on the sidelines, the manufacturing community does as well. "There are few in the mood to leverage themselves until they have a better sense of what to expect from the government and from the economy as a whole. Everything is more or less in place for expansion, but there has been no trigger thus far and there is plenty to make people more nervous about the future," said Kuehl.

Combined Manufacturing and Service Sectors (seasonally adjusted)	Jul '10	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun	Jul '11
Sales	57.2	57.6	58.6	60.8	61.9	65.9	63.5	66.3	64.7	64.5	59.4	60.8	60.0
New credit applications	54.1	54.6	54.8	56.8	58.2	60.1	58.6	60.3	59.8	58.8	58.2	56.7	57.3
Dollar collections	56.3	57.7	60.0	61.9	58.6	60.7	60.9	63.4	60.0	61.3	58.7	58.1	56.2
Amount of credit extended	56.0	57.1	58.7	59.8	61.2	61.7	64.8	66.5	64.4	64.7	62.1	60.4	62.0
Index of favorable factors	**55.9**	**56.7**	**58.0**	**59.8**	**60.0**	**62.1**	**62.0**	**64.1**	**62.2**	**62.3**	**59.6**	**59.0**	**58.9**
Rejections of credit applications	52.0	50.7	49.1	51.4	51.0	50.8	51.2	51.4	50.8	50.8	51.5	50.9	51.0
Accounts placed for collection	49.3	51.1	50.4	51.7	52.5	51.5	52.5	49.9	52.1	50.5	50.3	49.8	49.9
Disputes	50.6	50.9	50.8	49.9	50.8	49.2	51.0	49.2	48.9	49.3	48.8	49.3	50.0
Dollar amount beyond terms	49.4	47.0	49.1	50.9	48.9	53.4	51.5	50.6	49.7	50.7	46.5	49.9	48.3
Dollar amount of customer deductions	50.5	49.6	50.6	48.9	50.2	49.6	50.6	50.1	49.3	49.9	48.6	50.0	55.6
Filings for bankruptcies	55.0	56.9	55.7	57.0	56.3	55.4	59.1	56.0	57.4	58.1	58.1	56.5	55.8
Index of unfavorable factors	**51.1**	**51.0**	**50.9**	**51.6**	**51.6**	**51.7**	**52.6**	**51.2**	**51.4**	**51.5**	**50.6**	**51.0**	**51.7**
NACM Combined CMI	**53.0**	**53.3**	**53.8**	**54.9**	**55.0**	**55.8**	**56.4**	**56.4**	**55.7**	**55.8**	**54.2**	**54.2**	**54.6**



Manufacturing Sector

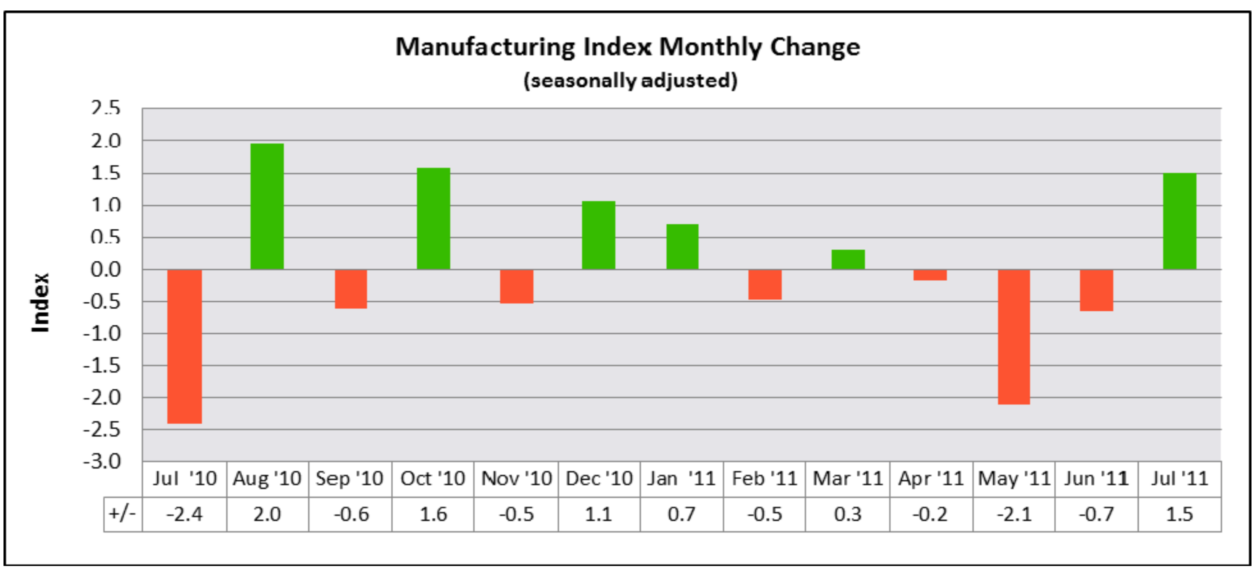
For the last two months, the manufacturing sector has been down and the service sector managed a decent recovery, but this month their positions seem to have reversed. There are signs that some enthusiasm in manufacturing has managed to return. Sales regained some lost momentum, although it is a long way from the 66.6 levels reached last December. While the sales data still falls below the 60 mark, it is up to 59.3 from the 58.5 posted last month. There was also a nice jump in the number of new credit applications—which rose from 54.5 to 56.4—but the level was at 60.6 just four months ago, so there remains a long way to go. Improvements were noted in the amount of credit extended as well—going from 59.2 to 61.2—and that was the only favorable category that crested above 60 this month. (In April all four of the manufacturing sector's favorable factors were above 60.) The overall gain in the favorable index went from 56.9 to 58.1. It doesn't alter the fact that in April it stood at 62.7 and in May it was still at 59.5. The trend is moving in the right direction, but there is ground to make up.

There was a bit of a mixed message when it came to manufacturing's unfavorable factors. On the one hand there was some really good news in terms of dollar amount of customer deductions, as the index moved from 49.5 to 61.2. This was by far the most dramatic change the index has seen in years. The highest this factor had been prior to this month was 50.1 in February; now it is well over 60. This alone tended to drag the whole set of unfavorable categories in a more positive direction. There were other minor improvements in areas such as disputes and bankruptcies. The index numbers that did not improve also didn't worsen much. This was a pretty steady state month in most respects. In total the index moved from 53.4 to 54.9 and that helped push the composite index into positive territory given the slump in the service sector readings.

The unusually high number in the customer deduction category is reinforced by the fact that many companies are not really having the kind of cash flow issues they reported earlier in the year. The point made by many analysts is that companies are sitting on their cash and that banks are sitting on their money as well—in part because there are few that are interested in a loan at the moment. This may be a further indication that the entire business community is in a wait-and-see mode. The numbers of bankruptcies are also down and that is yet another indicator that business is not really growing, but it isn't in big trouble yet either.

The good news is that manufacturers seem to be sitting on enough cash to handle their bills, for the moment. The bad news is that there is not much growth and at some point this lack of activity will start to cut into those reserves. Companies will have to either start growing their revenues and profits, or they will have to return to aggressive cost cutting and that means more job losses and another delay in demand.

Manufacturing Sector (seasonally adjusted)	Jul '10	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun	Jul '11
Sales	56.1	59.4	57.9	59.3	62.2	66.6	64.7	65.1	65.4	63.9	57.8	58.5	59.3
New credit applications	53.7	54.3	54.4	54.9	57.8	59.1	57.7	59.6	60.6	60.3	58.7	54.5	56.4
Dollar collections	53.0	60.1	61.1	61.0	57.9	60.5	60.3	61.5	60.8	60.2	60.1	55.3	55.4
Amount of credit extended	55.8	56.0	57.3	59.9	61.2	61.6	66.2	67.6	64.5	66.5	61.4	59.2	61.2
Index of favorable factors	**54.6**	**57.5**	**57.7**	**58.8**	**59.8**	**61.9**	**62.2**	**63.4**	**62.8**	**62.7**	**59.5**	**56.9**	**58.1**
Rejections of credit applications	52.0	52.6	49.6	53.2	52.1	51.3	52.0	51.9	51.6	51.0	52.6	51.8	50.8
Accounts placed for collection	48.5	52.8	51.9	53.6	52.7	51.1	53.0	51.2	53.9	50.7	50.7	49.8	49.4
Disputes	50.8	51.3	50.0	49.5	48.6	48.1	49.8	48.2	49.0	50.5	49.2	49.0	50.0
Dollar amount beyond terms	50.4	51.0	49.6	55.2	49.4	53.9	52.1	51.3	51.6	52.2	45.8	50.6	49.1
Dollar amount of customer deductions	49.9	48.4	49.4	48.5	48.8	49.4	49.1	50.1	48.8	49.5	47.7	49.5	61.2
Filings for bankruptcies	53.4	57.1	55.8	57.7	56.7	56.5	60.2	53.9	57.2	56.8	56.4	55.6	55.9
Index of unfavorable factors	**50.8**	**52.2**	**51.1**	**52.9**	**51.4**	**51.7**	**52.7**	**51.1**	**52.0**	**51.8**	**50.4**	**51.0**	**52.7**
NACM Manufacturing CMI	**52.4**	**54.3**	**53.7**	**55.3**	**54.7**	**55.8**	**56.5**	**56.0**	**56.3**	**56.1**	**54.0**	**53.4**	**54.9**



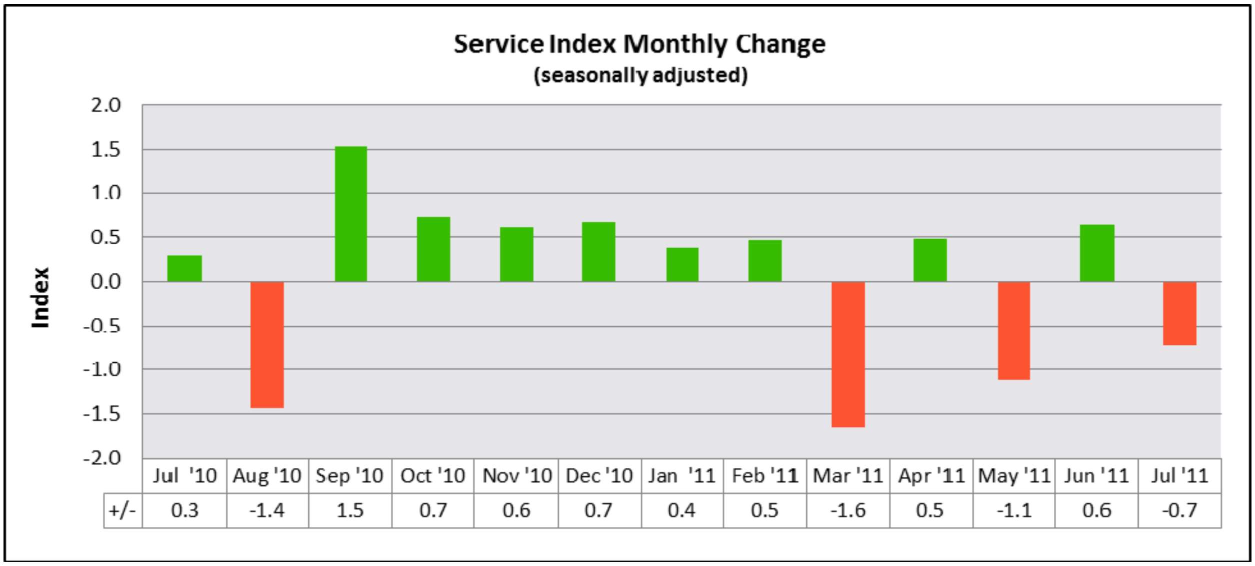
Service Sector

The service sector did not fare as well as manufacturing and managed to reverse some of the gains from the prior month. The big drop was in sales, as expected. The factor dropped from 63.2 to 60.7. The numbers are still above 60, but it has been receding since February when it hit 67.5. Given the large number of retailers that engage in the survey, this number is not shocking. Retail has been down for the past two months as the consumer has withdrawn again. The lack of progress on the job front has sent many people back into a cautious mode, and there is unlikely to be another burst of consumer activity until the attitude toward employment shifts again. The uncertainty at the government level has many people nervous as well, as they are hearing that one of the possible outcomes of the impasse will be a rise in interest rates. That makes people far less likely to spend and more likely to save in anticipation of the worst. The other favorable factors did not change all that much although there was a dip in dollar collections from 60.9 to 57.1.

Unfavorable factors dropped as well, but not drastically. The biggest problem seemed to be dollars beyond terms, which is consistent with the bad news coming out of retail. The summer selling season has been mediocre at best and all signs are pointing to a lackluster back-to-school sales season. The other piece of bad news is that there was a spike in the number of bankruptcies and that is rarely a good sign. The majority of these failures seem to be in the retail sector and in those industries that service the retail community, transportation included. There is a small silver lining behind the number of bankruptcies. The more that the system clears of uncompetitive stores and entities, the more market share is available for the survivors, but even those that have managed to make it through to this point really need to see demand come back to life sooner than later.

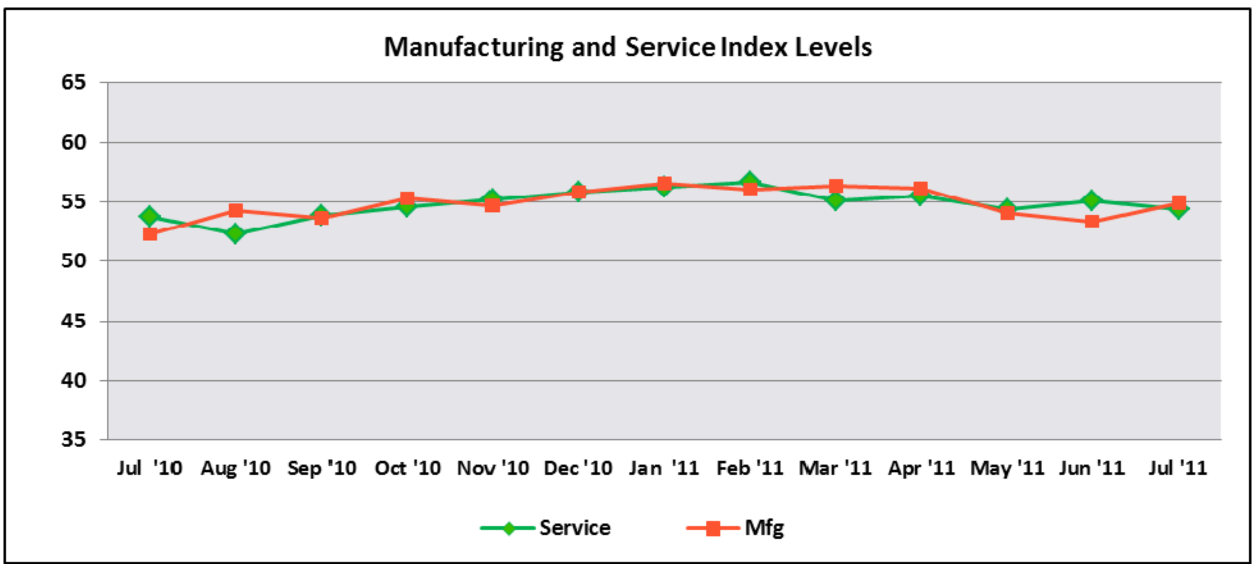
The overall service sector numbers are not catastrophic, but they are not inspiring by any stretch. The lack of consumer demand has been responsible for the drag on the sector and has made the majority of companies in this sector more vulnerable to the commodity price hikes that have been reminding people that inflation is not out of the question, even this year.

Service Sector (seasonally adjusted)	Jul '10	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun	Jul '11
Sales	58.2	55.7	59.3	62.2	61.6	65.1	62.3	67.5	63.9	65.0	61.1	63.2	60.7
New credit applications	54.5	54.8	55.1	58.7	58.6	61.1	59.4	61.0	59.0	57.3	57.8	58.8	58.2
Dollar collections	59.7	55.2	59.0	62.9	59.2	60.9	61.6	65.2	59.2	62.3	57.3	60.9	57.1
Amount of credit extended	56.3	58.1	60.0	59.6	61.2	61.8	63.4	65.4	64.2	63.0	62.7	61.6	62.7
Index of favorable factors	**57.2**	**56.0**	**58.4**	**60.9**	**60.2**	**62.2**	**61.7**	**64.8**	**61.6**	**61.9**	**59.7**	**61.1**	**59.7**
Rejections of credit applications	51.9	48.7	48.7	49.6	49.8	50.3	50.4	51.0	50.1	50.5	50.4	50.0	51.2
Accounts placed for collection	50.1	49.4	48.9	49.9	52.4	52.0	52.1	48.6	50.2	50.2	49.9	49.8	50.3
Disputes	50.5	50.5	51.5	50.3	52.9	50.3	52.1	50.1	48.7	48.1	48.5	49.6	50.0
Dollar amount beyond terms	48.4	43.1	48.5	46.6	48.5	52.9	51.0	49.9	47.8	49.2	47.3	49.1	47.5
Dollar amount of customer deductions	51.0	50.8	51.7	49.4	51.6	49.9	52.1	50.1	49.8	50.3	49.4	50.5	49.9
Filings for bankruptcies	56.6	56.6	55.5	56.3	55.9	54.3	57.9	58.2	57.7	59.5	59.8	57.3	55.8
Index of unfavorable factors	**51.4**	**49.8**	**50.8**	**50.4**	**51.8**	**51.6**	**52.6**	**51.3**	**50.7**	**51.3**	**50.9**	**51.0**	**50.8**
NACM Service CMI	**53.7**	**52.3**	**53.8**	**54.6**	**55.2**	**55.8**	**56.2**	**56.7**	**55.1**	**55.5**	**54.4**	**55.1**	**54.3**



July 2011 vs. July 2010

The year-over-year numbers are still swapping places month to month. The last survey showed a big gain in the service sector, and now that gain has been lost and manufacturers are seeing some of that growth. The good news remains that the numbers are still in the mid-50s, but the bad news is that they have been stuck in the same position for over a year. By now one would have hoped to see a steady uphill trend and that has not manifested.



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:

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

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 16,000 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. 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.

This report and the CMI archives may be viewed at http://web.nacm.org/cmi/cmi.asp.

Source: National Association of Credit Management

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