Report for June 2011

Issued June 30, 2011

National Association of Credit Management

Combined Sectors

The overall economic narrative in the country for the last month has been a question as to whether the latest run of bad economic news is a temporary phenomenon or is the harbinger of much worse to come. As many analysts have asserted that this is all attributable to the earthquake and "Arab Spring" as those who assert a double-dip recession is setting up for as early as the third quarter. Most of the economic community is somewhere in between, but much of the interpretation lies within the latest run of data, and the National Association of Credit Management's (NACM) Credit Managers' Index (CMI) for June suggests the temporary impact position has some validity.

The dramatic collapse reflected in the May CMI eased up a little in June. The index numbers bounced around, but these variations were obscured somewhat by the fact that the index as a whole was flat. Considering this month, it is very apparent that the devil is in the details. The overall index number was exactly the same as it was in May—54.2—but there were significant changes in the combined sub-indices for favorable and unfavorable factors.

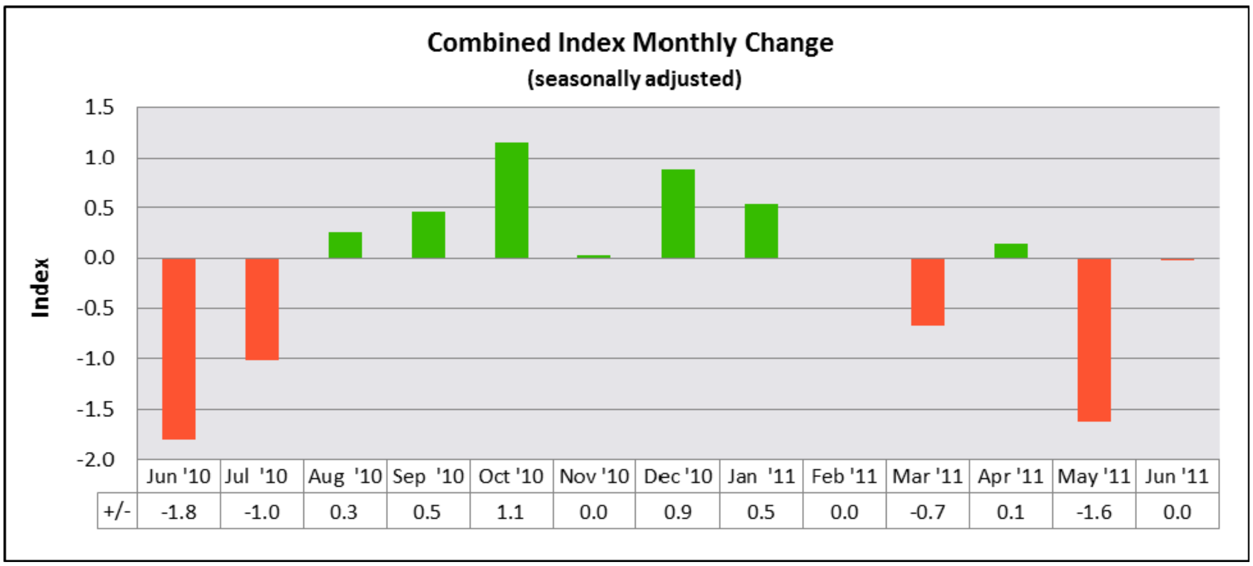
"The most distressing news comes from the number of credit applications received and the amount of credit extended," said Chris Kuehl, PhD, managing director of Armada Corporate Intelligence and NACM economic advisor. Many businesses seemed more cautious in the last month or so. Part of this is still related to the issues in Japan and the fear of higher commodity prices, but there is also some growing unease regarding political games. "Few really believe that the United States would put $100 billion at risk in its securities market by not raising the debt limit, but there is intense fear that Congress will take the game too far and provoke a reaction in the markets before it reaches an agreement," Kuehl said. "It appears this trepidation is affecting the willingness of businesses to expand and seek additional credit. The good news is that sales have risen during this period; in the past, expanded sales usually beget more credit requests and more credit extended."

The bad news in favorable factors has been balanced out by good news in some of the unfavorable factors. Many signs of distress weakened a little. There were fewer disputes and fewer dollars beyond terms. While there were also fewer bankruptcies, there were still concerns about the number of credit applications rejected and the number of accounts placed for collection. "The overall impression is that there is some separation taking place between those companies that have weathered the last few years and those that had been counting on an economic breakthrough to help salvage their financial position. This is a development we've referenced before and the pattern is still evident," said Kuehl.

As the recession gives way to a slow recovery there is a series of expected moves from the different players in a given industry sector. The market leaders start to anticipate the end of the downturn, and they are ready to ramp up and make an attempt to grab market share from rivals. The best-prepared companies make the first moves forcing competitors to try to keep pace. Some do, but others begin to falter as the business they expected to cover their investment fails to materialize. Right below the market leader category is the market challenger and they are looking for the weak link among the market leaders. They push with their own expansion schemes in an attempt to supplant them. If they calculate correctly they make the jump; if they do not they fall back and start to struggle with cash flow. Right behind the leaders and the challengers are the market followers and they are waiting to see how the bigger battles play out before they choose which approach to emulate.

"Right now the economic recovery is waiting for the market followers to make their move. This is the biggest category of business—and the most cautious," said Kuehl. The CMI data suggest that this sector is starting to have more active sales activity, which generally provokes more credit demand. The majority of credit requests have been coming from either the most important customers with the best credit or from those struggling on the bottom tier. "When the middle levels start to get earnestly engaged is when there is potential for more general overall economic growth."

Combined Manufacturing and Service Sectors (seasonally adjusted)	Jun '10	Jul	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun '11
Sales	59.0	57.2	57.6	58.6	60.8	61.9	65.9	63.5	66.3	64.7	64.5	59.4	60.8
New credit applications	57.4	54.1	54.6	54.8	56.8	58.2	60.1	58.6	60.3	59.8	58.8	58.2	56.7
Dollar collections	59.4	56.3	57.7	60.0	61.9	58.6	60.7	60.9	63.4	60.0	61.3	58.7	58.1
Amount of credit extended	55.9	56.0	57.1	58.7	59.8	61.2	61.7	64.8	66.5	64.4	64.7	62.1	60.4
Index of favorable factors	**57.9**	**55.9**	**56.7**	**58.0**	**59.8**	**60.0**	**62.1**	**62.0**	**64.1**	**62.2**	**62.3**	**59.6**	**59.0**
Rejections of credit applications	51.0	52.0	50.7	49.1	51.4	51.0	50.8	51.2	51.4	50.8	50.8	51.5	50.9
Accounts placed for collection	51.4	49.3	51.1	50.4	51.7	52.5	51.5	52.5	49.9	52.1	50.5	50.3	49.8
Disputes	50.4	50.6	50.9	50.8	49.9	50.8	49.2	51.0	49.2	48.9	49.3	48.8	49.3
Dollar amount beyond terms	49.1	49.4	47.0	49.1	50.9	48.9	53.4	51.5	50.6	49.7	50.7	46.5	49.9
Dollar amount of customer deductions	50.3	50.5	49.6	50.6	48.9	50.2	49.6	50.6	50.1	49.3	49.9	48.6	50.0
Filings for bankruptcies	56.6	55.0	56.9	55.7	57.0	56.3	55.4	59.1	56.0	57.4	58.1	58.1	56.5
Index of unfavorable factors	**51.5**	**51.1**	**51.0**	**50.9**	**51.6**	**51.6**	**51.7**	**52.6**	**51.2**	**51.4**	**51.5**	**50.6**	**51.0**
NACM Combined CMI	**54.1**	**53.0**	**53.3**	**53.8**	**54.9**	**55.0**	**55.8**	**56.4**	**56.4**	**55.7**	**55.8**	**54.2**	**54.2**



Manufacturing Sector

When manufacturing fell so dramatically last month there was a lot of conjecture as to what had caused the sudden interruption of a sector that had been performing so well up to this point. It has been unusual but consistent. Manufacturing has been pulling the economy along for the bulk of the recovery on the strength of export demand from the emerging market nations and on the strength of the business community's decision to start adding more and more inventory in anticipation of a more widespread gain in demand as the consumer came out of their funk. Retail numbers looked pretty good at the start of the year and optimism was gaining some momentum. That all seemed to come screeching to a halt in May and the question was whether this was the beginning of the end of the stunning run for the manufacturing sector or just a reaction to all the turmoil since the first of the year.

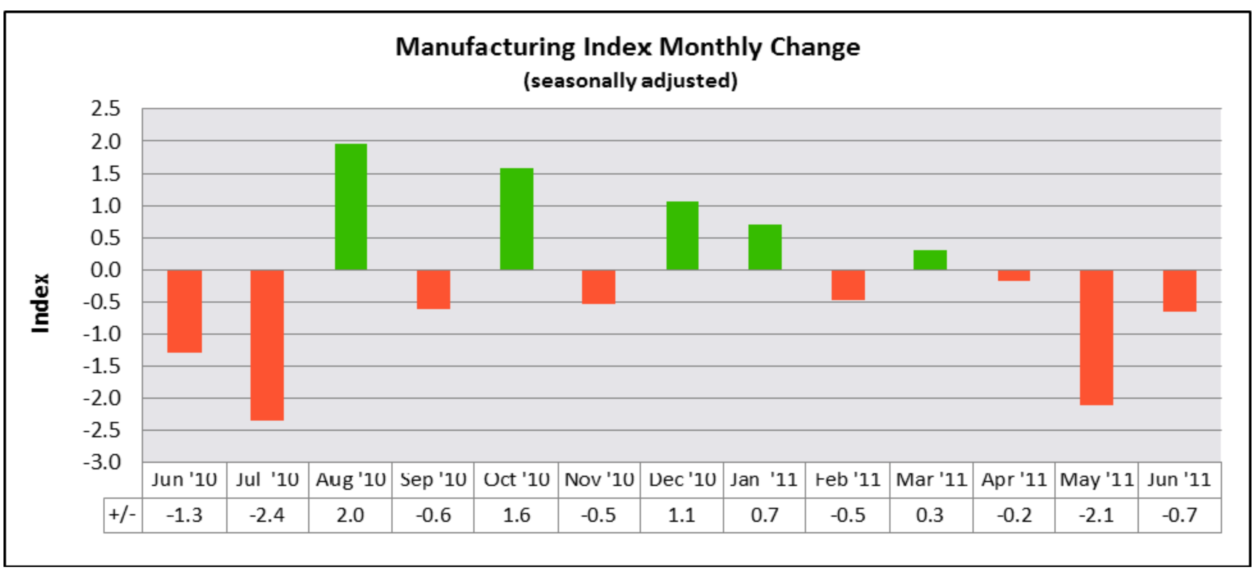
The jury remains divided. On the positive side, manufacturing categories showed solid recovery in some critical areas, but on the negative side there were some obvious challenges remaining. May's precipitous drop was ameliorated to some degree in June, but there was nothing suggesting full recovery either. The index of favorable factors fell pretty hard again and the index level is now as low as it as last July; not the trend many had been hoping for. The only factor that improved was sales and that is an encouraging sign for those hoping to see manufacturers get back in the swing of things. The real problems showed up in factors like new credit applications, which were down from 58.7 to 54.5. Dollar collections also dropped from 60.1 to 55.3, which is not encouraging. The amount of credit extended slumped as well.

The total decline in favorable factors is discouraging – going from 59.5 to 56.9. The good news in these otherwise bleak numbers is that the sectors are all still above 50 and the sales readings are improving.

News in unfavorable factors wasn't as bad and some factors showed improvement. Dollars beyond terms picked up from 45.8 to 50.6 and got back into the expansion category after languishing in contraction. Overall, the index of unfavorable categories gained slightly, from 50.4 to 51. That is still very narrow and barely keeps this sector in expansion territory, but the point is that sector seems to have survived the more harrowing moments of the year thus far. The fact remains that manufacturing is not as robust as one would prefer, but remains just in the expansion realm.

When one looks at the manufacturing numbers from the Purchasing Managers Index and other data points, such as durable goods orders and factory orders, it is apparent that the industrial community was on hold for the last two months. The extent to which this is result of the Japanese triple disaster and the spike in oil and other commodity prices remains to be seen, but on the basis of this data it would appear that some of the temporary influences have faded. Now the ball is back in the consumer's court. If demand starts to pick up the pace, the current accumulated inventory will be exhausted and there will be a resumption of production. That remains a very big "if."

Manufacturing Sector (seasonally adjusted)	Jun '10	Jul	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun '11
Sales	59.1	56.1	59.4	57.9	59.3	62.2	66.6	64.7	65.1	65.4	63.9	57.8	58.5
New credit applications	58.9	53.7	54.3	54.4	54.9	57.8	59.1	57.7	59.6	60.6	60.3	58.7	54.5
Dollar collections	59.0	53.0	60.1	61.1	61.0	57.9	60.5	60.3	61.5	60.8	60.2	60.1	55.3
Amount of credit extended	58.2	55.8	56.0	57.3	59.9	61.2	61.6	66.2	67.6	64.5	66.5	61.4	59.2
Index of favorable factors	**58.8**	**54.6**	**57.5**	**57.7**	**58.8**	**59.8**	**61.9**	**62.2**	**63.4**	**62.8**	**62.7**	**59.5**	**56.9**
Rejections of credit applications	51.8	52.0	52.6	49.6	53.2	52.1	51.3	52.0	51.9	51.6	51.0	52.6	51.8
Accounts placed for collection	54.3	48.5	52.8	51.9	53.6	52.7	51.1	53.0	51.2	53.9	50.7	50.7	49.8
Disputes	50.6	50.8	51.3	50.0	49.5	48.6	48.1	49.8	48.2	49.0	50.5	49.2	49.0
Dollar amount beyond terms	50.3	50.4	51.0	49.6	55.2	49.4	53.9	52.1	51.3	51.6	52.2	45.8	50.6
Dollar amount of customer deductions	49.2	49.9	48.4	49.4	48.5	48.8	49.4	49.1	50.1	48.8	49.5	47.7	49.5
Filings for bankruptcies	55.6	53.4	57.1	55.8	57.7	56.7	56.5	60.2	53.9	57.2	56.8	56.4	55.6
Index of unfavorable factors	**52.0**	**50.8**	**52.2**	**51.1**	**52.9**	**51.4**	**51.7**	**52.7**	**51.1**	**52.0**	**51.8**	**50.4**	**51.0**
NACM Manufacturing CMI	**54.7**	**52.4**	**54.3**	**53.7**	**55.3**	**54.7**	**55.8**	**56.5**	**56.0**	**56.3**	**56.1**	**54.0**	**53.4**



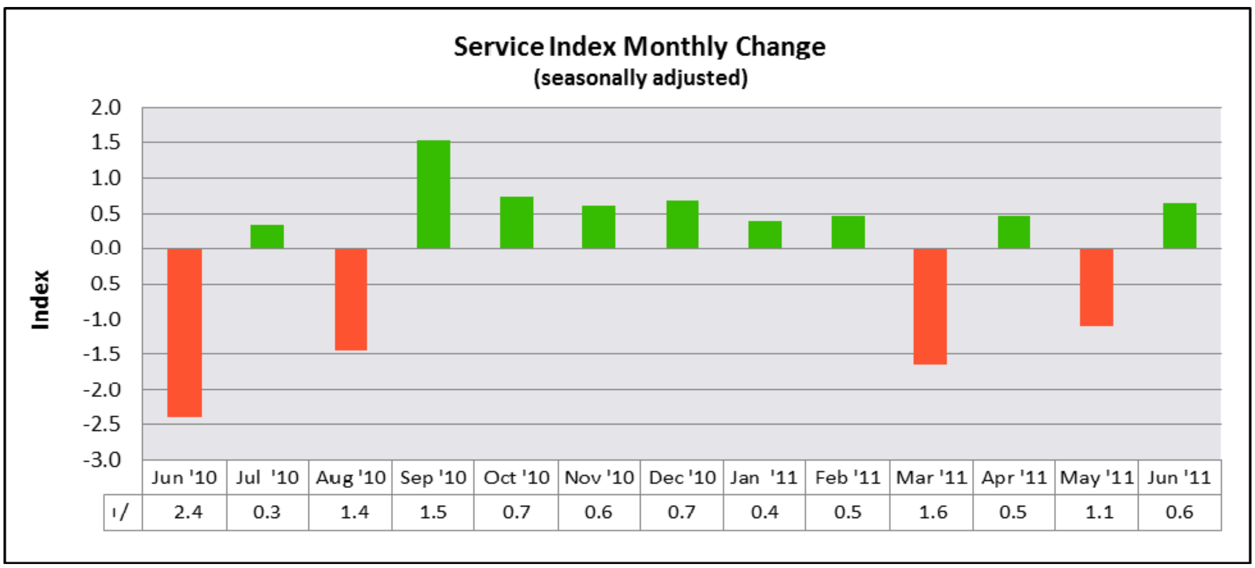
Service Sector

The service sector performance is encouraging. The index of favorable factors broke above 60 again, jumping from 59.7 to 61.1, but remains below the February's level when the retail community made a push. The impetus for the jump seemed to come from a variety of factors. Sales returned to March levels, moving from 61.1 to 63.2. There were more credit applications and more dollars collected, while the amount of credit extended declined a little from 62.7 to 61.6. This is still respectable, however, and keeps the credit extended number above 60 for the eighth straight month.

Unfavorable factor news was pretty good as well. Overall, the index gained, improving from 50.9 to 51. This is not spectacular by any means, but a positive trend is a positive trend. The best news came from the decline in disputes and dollar amounts of customer deductions. Part of the ongoing concern as far as the unfavorable factors are concerned is that three of the six factors are still below the 50 threshold signaling growth. The good news is that last month there were four factors below 50. This month the dollar amount of customer deductions moved from 49.4 to 50.5.

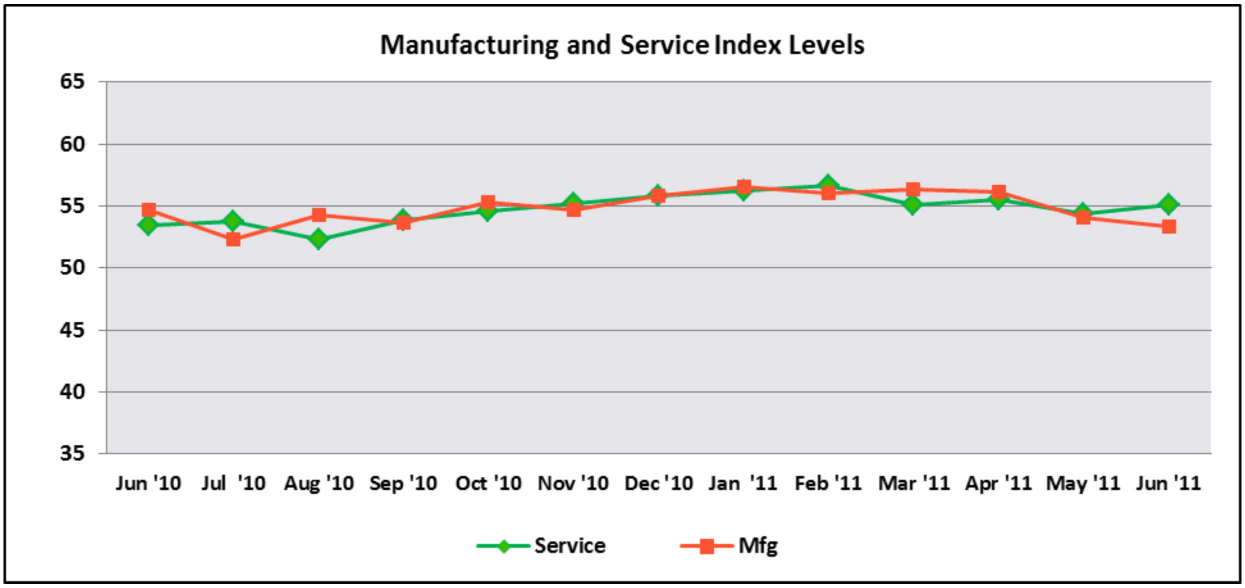
The service sector is varied and it is always hard to determine what is really moving, but the evidence points to gains in health care and professional services and a mixed bag as far as retail is concerned. The one common denominator in most areas is that growth is dependent on domestic demand as opposed to demand from the exports. The strength of the U.S. economy as a whole is measured to a significant degree by the strength of the service side of the economy and this data would suggest that there is more recovery taking place than in previous months.

Service Sector (seasonally adjusted)	Jun '10	Jul	Aug	Sep	Oct	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun '11
Sales	58.8	58.2	55.7	59.3	62.2	61.6	65.1	62.3	67.5	63.9	65.0	61.1	63.2
New credit applications	55.9	54.5	54.8	55.1	58.7	58.6	61.1	59.4	61.0	59.0	57.3	57.8	58.8
Dollar collections	59.7	59.7	55.2	59.0	62.9	59.2	60.9	61.6	65.2	59.2	62.3	57.3	60.9
Amount of credit extended	53.7	56.3	58.1	60.0	59.6	61.2	61.8	63.4	65.4	64.2	63.0	62.7	61.6
Index of favorable factors	**57.0**	**57.2**	**56.0**	**58.4**	**60.9**	**60.2**	**62.2**	**61.7**	**64.8**	**61.6**	**61.9**	**59.7**	**61.1**
Rejections of credit applications	50.3	51.9	48.7	48.7	49.6	49.8	50.3	50.4	51.0	50.1	50.5	50.4	50.0
Accounts placed for collection	48.5	50.1	49.4	48.9	49.9	52.4	52.0	52.1	48.6	50.2	50.2	49.9	49.8
Disputes	50.3	50.5	50.5	51.5	50.3	52.9	50.3	52.1	50.1	48.7	48.1	48.5	49.6
Dollar amount beyond terms	47.9	48.4	43.1	48.5	46.6	48.5	52.9	51.0	49.9	47.8	49.2	47.3	49.1
Dollar amount of customer deductions	51.4	51.0	50.8	51.7	49.4	51.6	49.9	52.1	50.1	49.8	50.3	49.4	50.5
Filings for bankruptcies	57.6	56.6	56.6	55.5	56.3	55.9	54.3	57.9	58.2	57.7	59.5	59.8	57.3
Index of unfavorable factors	**51.0**	**51.4**	**49.8**	**50.8**	**50.4**	**51.8**	**51.6**	**52.6**	**51.3**	**50.7**	**51.3**	**50.9**	**51.0**
NACM Service CMI	**53.4**	**53.7**	**52.3**	**53.8**	**54.6**	**55.2**	**55.8**	**56.2**	**56.7**	**55.1**	**55.5**	**54.4**	**55.1**



June 2011 vs. June 2010

The year-over-year numbers are divergent this month as there was more progress on the service side than in manufacturing. The data is still putting the index above 50, but growth is anemic. This is not the kind of news that sends people into celebration, but neither is it depressing. The good news is that the index has been over 50 and in expansion territory for 18 months thus far.



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.

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