Report for May 2010

Issued June 1, 2010

National Association of Credit Management

Combined Sectors

There has been a great deal of concern in the financial sector in the last month as the world reacts to the mounting threats from the "Greek disease." While it has been acknowledged that the crisis is disrupting the markets in Europe as well as the rest of the world, there has been relatively little impact on the rest of the global economy to this point. The data from May's Credit Managers' Index, issued by the National Association of Credit Management (NACM), seem to suggest that this turmoil is having an impact on the U.S. credit and business community—perhaps more than most people realize.

"Over the last few years the CMI has tended to be a harbinger of things to come as far as the overall economy is concerned as it presages the activity in the credit and financial communities," said Chris Kuehl, Ph.D., NACM economic advisor, who prepares the CMI report each month. The CMI dipped in 2008, three months before the rest of the economy started to react to the banking debacle that engulfed the U.S. and the rest of the world soon after. Now the CMI is dipping again—and dramatically—while at the same time the rest of the economic indicators have barely started to respond. "The sense among observers has been that the Greek crisis and its implications would soon have the same kind of impact on the credit environment that the sub-prime crisis had in 2008. Last month's data seems to bear this out."

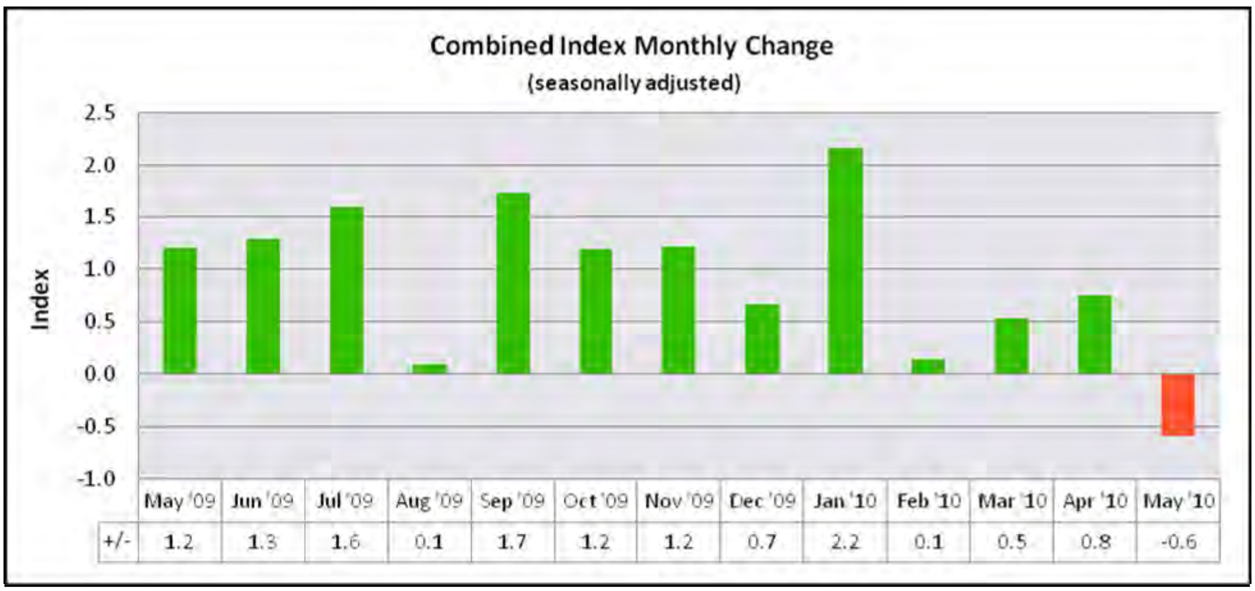
Kuehl noted the growing signs of distress in credit circles in the last few weeks, the most obvious being the rise of the London Interbank Offered Rate (LIBOR) to a point not seen since July 2009. The LIBOR is the benchmark for banks making short-term loans to one another and often determines the rates that drive the rest of the economy, more so than the interest rates set by central banks. "A growing concern among bondholders, about the viability of the European economy, has caused some wild swings in both bonds and equities," said Kuehl. "The data from the CMI is both reflecting this and anticipating some more trouble in the future."

There has been deterioration in both the positive and negative factors across the board, although the service sector has been hit harder than manufacturing. Sales have slipped from 65.7 to 64.5 which is not a dramatic reduction, but comes after five months of steady increases. The level of dollar collections fell as well—from 62.1 to 59.7—as some business sectors struggled to keep pace with the nascent recovery. There was also a reduction in the level of credit as the financial system tightened again.

Some of the more urgent changes took place in the negative categories. The dollar amount of customer deductions fell from 55.7 to 51.8. There is a sense that accounts have become nervous again and have started to worry about their access to capital in the coming months as well as their ability to keep generating sufficient demand to maintain their growth expectations. "There is not the level of panic that existed in the months leading up to the credit meltdown, but there is far more concern about what is happening in the global markets than existed even a few weeks ago," said Kuehl. "The fact that the major concern is rooted in Europe is slightly better news than if it were motivated by another meltdown in the U.S., but it is entirely possible that the Greek disease will spread."

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)	May '09	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10	Feb	Mar	Apr	May '10
Sales	41.8	44.8	48.6	48.4	49.9	51.1	55.0	56.7	60.7	60.9	65.0	65.7	64.5
New credit applications	48.2	50.7	52.6	49.3	50.0	52.7	55.4	54.2	57.0	57.7	57.5	57.4	58.6
Dollar collections	48.8	51.2	50.8	50.5	53.4	54.7	55.8	58.0	61.3	61.1	61.9	62.1	59.7
Amount of credit extended	44.3	46.1	48.2	48.0	49.3	53.6	54.6	55.2	58.8	59.4	61.3	61.3	60.2
Index of favorable factors	**45.8**	**48.2**	**50.0**	**49.1**	**50.6**	**53.0**	**55.2**	**56.0**	**59.4**	**59.8**	**61.4**	**61.6**	**60.7**
Rejections of credit applications	47.4	47.9	47.5	49.0	48.4	49.0	49.3	50.1	51.4	51.0	50.1	50.9	50.7
Accounts placed for collection	40.2	40.5	44.0	43.6	45.3	47.1	49.5	50.9	50.7	50.4	51.1	50.6	54.5
Disputes	47.5	47.7	50.2	49.7	50.8	51.0	49.6	51.0	51.4	52.2	52.2	51.7	51.3
Dollar amount beyond terms	43.4	43.6	45.3	46.2	48.1	48.1	49.0	51.4	52.2	52.0	51.5	51.9	50.2
Dollar amount of customer deductions	47.5	48.9	49.2	50.6	51.8	50.5	51.3	51.3	52.5	51.2	51.7	55.7	51.8
Filings for bankruptcies	42.3	42.8	43.7	45.8	51.5	52.6	53.0	50.5	54.7	56.3	55.3	57.6	57.6
Index of unfavorable factors	**44.7**	**45.2**	**46.7**	**47.5**	**49.3**	**49.7**	**50.3**	**50.8**	**52.2**	**52.2**	**52.0**	**53.1**	**52.7**
NACM Combined CMI	**45.1**	**46.4**	**48.0**	**48.1**	**49.8**	**51.0**	**52.3**	**52.9**	**55.1**	**55.2**	**55.7**	**56.5**	**55.9**



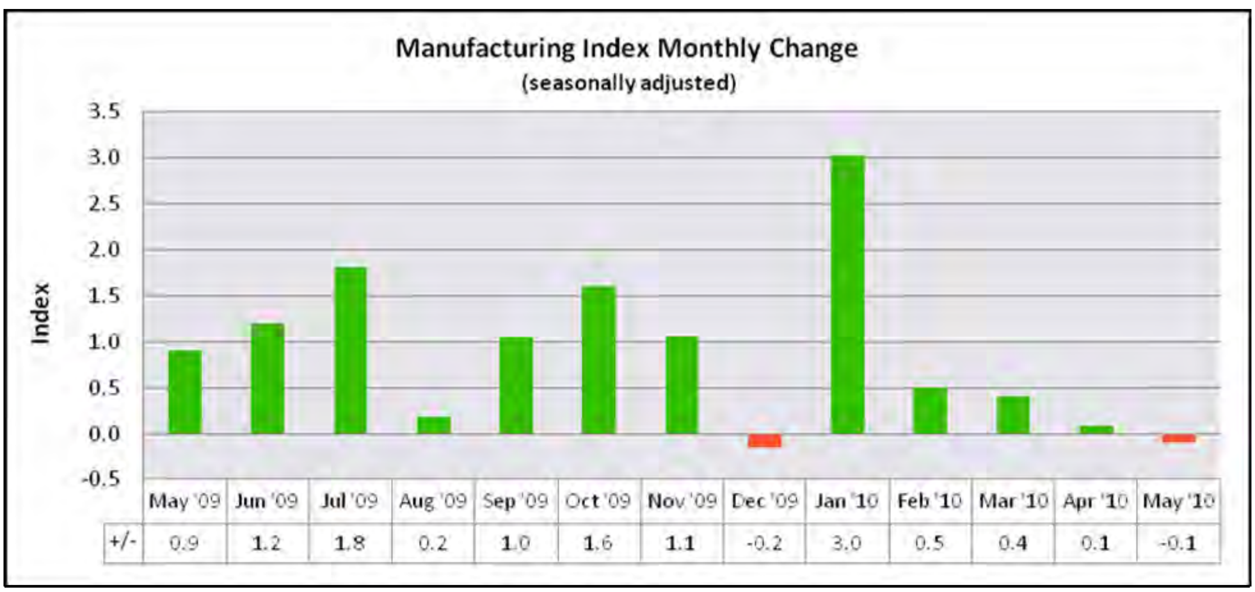
Manufacturing Sector

Over the last few months the manufacturing sector has been in the unusual position of being the lead dog in the economic recovery. This is a circumstance not slated to last and really can't unless the consumer gets engaged again. The rise of the industrial sector started in the latter part of 2009 as companies anticipated the rise of the economy in 2010. To meet that demand and protect market share positions, manufacturers started to build inventory positions and waited. "The data support the notion that manufacturers started to grow during this period—capacity utilization improved at the same time that productivity gains continued," said Kuehl. "This led to GDP growth of nearly 6% in the last quarter of 2009. That is the first step in a recovery, however, and without the engagement of the consumer, the manufacturer will soon sink back to pre-inventory build levels."

The CMI suggests there is still some energy left in the sector as sales continue to grow, although not at the pace of the past few months. The amount of credit extended saw the most serious decline in the favorable factors, falling from 62.1 to 58.9, another indication credit markets have tightened again. There has been an expansion of new credit applications, so the demand is still there, but the willingness to extend the credit has become more constrained. The big changes in terms of negative factors involved disputes, bankruptcies and accounts placed for collection. These problems suggest that some of the manufacturers not able to ramp up to compete with those anticipating the market's expansion are now starting to fall by the wayside. This was expected, Kuehl noted. Coming out of a recession is very often the riskiest position for many companies that had been struggling to get through the downturn.

For the most part, the manufacturing sector stayed where it was last month—shifting down slightly from 56.1 to 56. There is still some solid good news, but the entire sector has essentially stagnated in the last three months as it waits for the entire economy to catch up and create some new demand to soak up the inventory production that may have originally launched the recovery.

Manufacturing Sector (seasonally adjusted)	May '09	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10	Feb	Mar	Apr	May '10
Sales	40.7	45.4	48.7	48.4	48.7	52.0	56.3	55.8	61.8	62.5	66.9	65.2	66.0
New credit applications	49.3	51.1	55.3	48.6	50.5	52.9	56.8	55.2	54.0	57.8	57.9	57.1	58.9
Dollar collections	47.5	51.6	51.7	51.3	52.1	55.7	53.1	56.0	61.5	59.6	61.4	60.9	59.7
Amount of credit extended	44.2	45.8	49.3	48.9	48.8	53.5	53.4	55.2	59.2	60.7	62.0	62.1	58.9
Index of favorable factors	**45.4**	**48.5**	**51.3**	**49.3**	**50.0**	**53.5**	**54.9**	**55.6**	**59.1**	**60.2**	**62.1**	**61.3**	**60.9**
Rejections of credit applications	47.4	47.8	47.5	50.6	48.9	49.6	49.5	49.5	52.4	51.4	50.9	52.3	51.6
Accounts placed for collection	41.8	41.2	44.1	43.3	46.3	47.1	49.5	51.0	51.3	51.0	51.9	52.0	54.3
Disputes	47.6	46.1	49.3	48.2	49.5	50.9	48.0	50.1	50.7	51.9	51.5	51.8	50.0
Dollar amount beyond terms	44.5	45.3	46.3	48.1	48.3	47.9	50.0	51.4	52.5	53.3	51.3	52.2	50.1
Dollar amount of customer deductions	46.6	47.6	47.8	50.4	50.8	49.9	50.3	49.8	52.2	51.3	51.6	50.8	51.0
Filings for bankruptcies	43.6	43.2	43.1	47.3	51.7	52.1	55.4	46.6	55.4	56.5	54.8	56.6	59.5
Index of unfavorable factors	**45.2**	**45.2**	**46.4**	**48.0**	**49.2**	**49.6**	**50.4**	**49.7**	**52.4**	**52.6**	**52.0**	**52.6**	**52.7**
NACM Manufacturing CMI	**45.3**	**46.5**	**48.3**	**48.5**	**49.6**	**51.2**	**52.2**	**52.1**	**55.1**	**55.6**	**56.0**	**56.1**	**56.0**



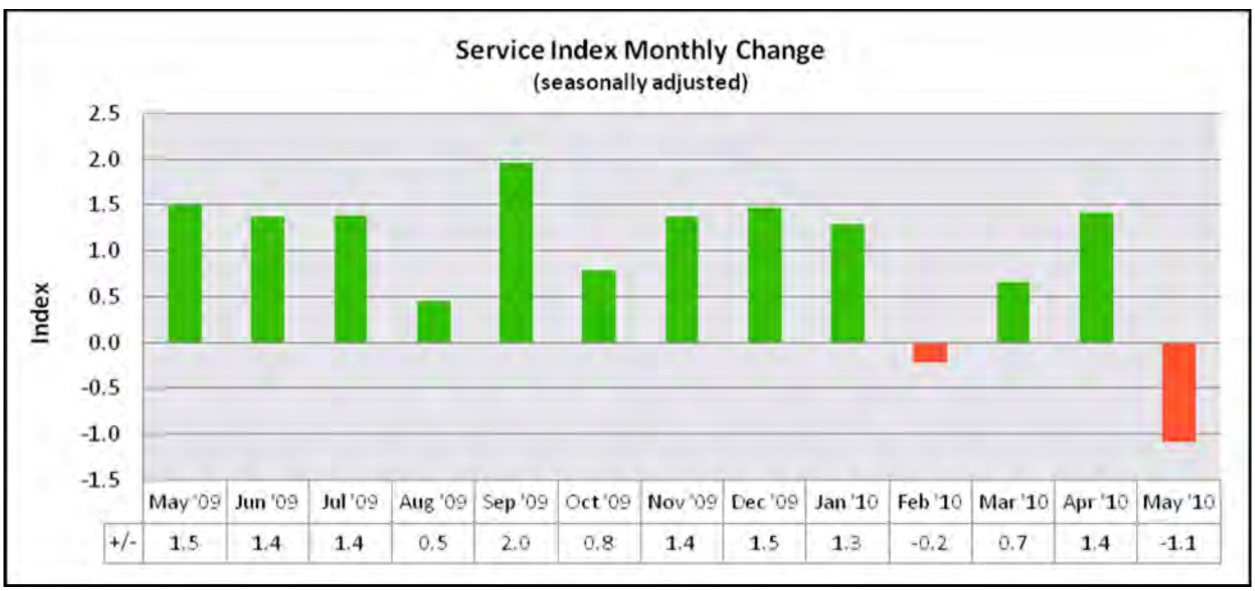
Service Sector

"The most worrisome part of this month's CMI is the performance of the service sector," said Kuehl. "This is the reason that the entire index took such a dip, and the problems that are suggested by this data will reverberate through the greater economy in months to come. The impact of the service sector on the economy as a whole has been well documented over the years—80% of job growth, 80% of the growth in GDP." The declines in this month's index were in both the positive and negative categories. Sales fell from 66.3 to 63, despite the fact that there were generally some solid gains in the retail community. "This means that other elements of the service sector have been suffering," he said. The drop in dollar collections was serious as well—from 63.2 to 59.7. It appears that a lot of this came from the suddenly stressed financial sector.

One of the biggest falls took place in dollar amount of customer deductions—moving from 60.5 to 52.6. There was also a big drop in bankruptcy numbers—from 58.6 to 55.7. The entire service sector appears under stress and much of this nervousness can be attributed to consternation in global stock markets. As the European debt crisis unfolds, the most threatened sectors are generally those in the service categories, everything from the financial community to general professional business. The numbers from retail have been solid, but are cause for alarm as the CMI traditionally anticipates downturns by a month or so.

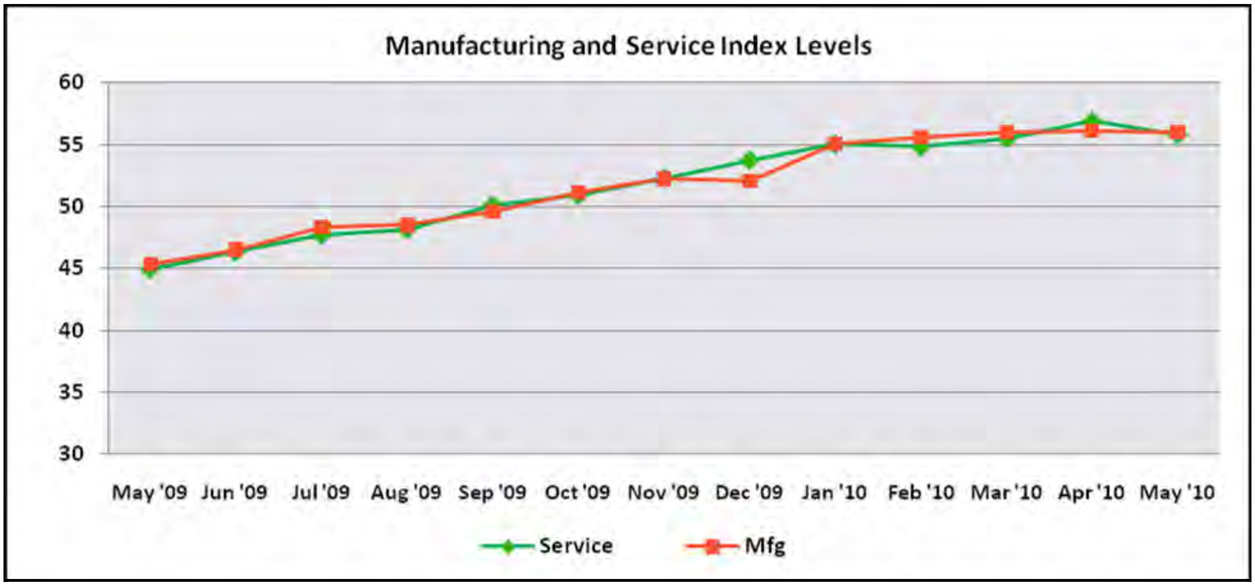
"If consumers really are starting to fade and withdraw from the patterns they have only recently resumed, the manufacturing community will feel the decline sooner than later," said Kuehl.

Service Sector (seasonally adjusted)	May '09	Jun	Jul	Aug	Sep	Oct	Nov	Dec '09	Jan '10	Feb	Mar	Apr	May '10
Sales	42.9	44.1	48.4	46.5	51.0	50.3	53.7	57.5	59.6	59.3	63.0	66.3	63.0
New credit applications	47.2	50.3	49.9	49.5	49.5	52.4	54.1	53.2	60.1	57.6	57.1	57.7	58.2
Dollar collections	50.0	50.8	49.8	50.5	54.8	53.7	58.6	59.9	61.2	62.7	62.4	63.2	59.7
Amount of credit extended	44.3	46.4	47.1	46.3	49.8	53.8	55.7	55.2	58.3	58.2	60.5	60.5	61.5
Index of favorable factors	**46.1**	**47.9**	**48.8**	**48.2**	**51.2**	**52.5**	**55.5**	**56.5**	**59.8**	**59.4**	**60.8**	**62.0**	**60.6**
Rejections of credit applications	47.4	48.1	47.4	48.5	47.9	48.5	49.2	50.6	50.4	50.6	49.4	49.6	49.7
Accounts placed for collection	38.7	39.8	43.9	43.7	44.3	47.1	49.4	50.7	50.1	49.9	50.2	49.2	54.8
Disputes	47.3	49.4	51.2	49.0	52.1	51.0	51.2	51.9	52.1	52.5	52.9	51.6	52.7
Dollar amount beyond terms	42.3	41.9	44.3	49.5	47.9	48.3	48.0	51.4	51.9	50.6	51.6	51.7	50.3
Dollar amount of customer deductions	48.4	50.2	50.7	51.1	52.7	51.1	52.3	52.7	52.9	51.1	51.8	60.5	52.6
Filings for bankruptcies	41.0	42.3	44.4	47.0	51.3	53.0	50.7	54.3	53.9	56.0	55.8	58.6	55.7
Index of unfavorable factors	**44.2**	**45.3**	**47.0**	**48.1**	**49.4**	**49.8**	**50.1**	**52.0**	**51.9**	**51.8**	**52.0**	**53.5**	**52.6**
NACM Service CMI	**45.0**	**46.3**	**47.7**	**48.2**	**50.1**	**50.9**	**52.3**	**53.8**	**55.0**	**54.8**	**55.5**	**56.9**	**55.8**



May 2010 vs. May 2009

The CMI remains comfortably above 50 and in the expansion category, but the relentless march toward 60 has been interrupted and the difference between the CMI and the Purchasing Managers Index (PMI) is as wide as it has been in some months. “If the CMI pattern holds, the next month or so will show a decline in the PMI numbers, unless there is a recovery in the CMI by the July release. This stutter in the progress of the CMI is of real concern, but the extent of the decline will not be known until there is a trend that extends beyond one month,” said Kuehl.



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 near the end 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

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.

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

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