Report for May 2014

Issued May 30, 2014

National Association of Credit Management

Combined Sectors

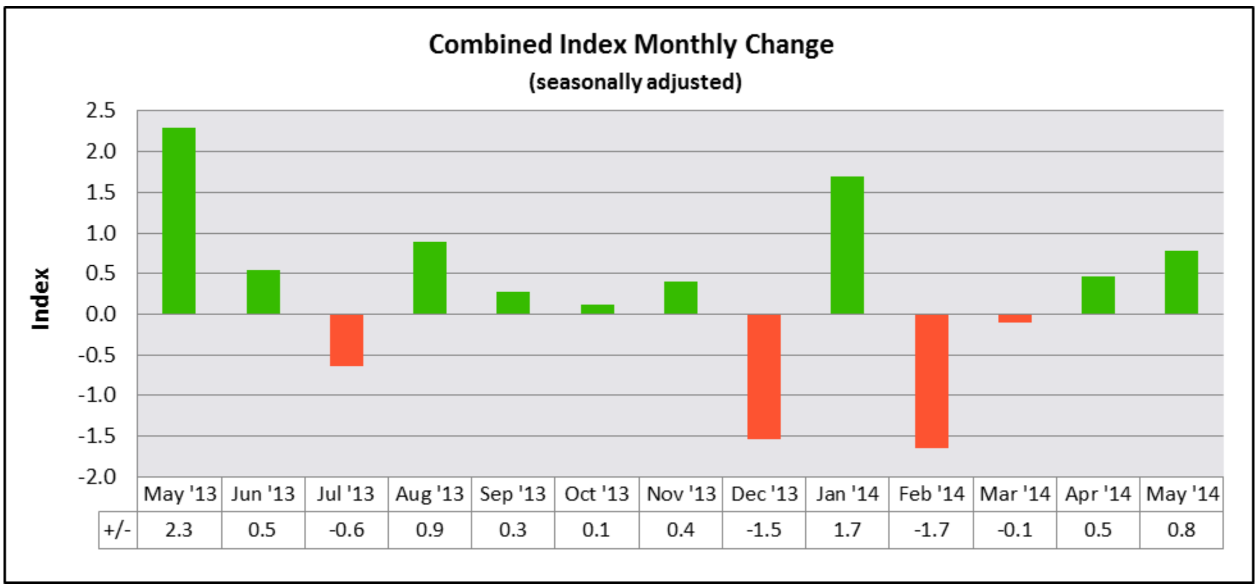
The latest revision of the GDP numbers showed that the country trended negatively by 1% and by the time the third revision of the GDP is released in a few weeks, the news could be even worse. "The poor performance of the economy is now official," said NACM Economist Chris Kuehl, PhD. "However, those watching the Credit Managers' Index (CMI) issued by the National Association of Credit Management (NACM) already knew this; all it would have taken is a cursory look at the declines in the combined index since the start of the year as it slipped from a nice start of 57.3 to levels not seen since July of last summer, with March hitting a number as low as the index had seen in the last 12 months. The good news recently as far as economic analysis is concerned is that the economy seems to be in the midst of a nice recovery and most think that the second quarter data will be far stronger than the first's. The May report of the CMI would seem to reinforce this notion as the combined CMI is back up to 56.8, the third-highest mark reached in the last 12 months. The sense of recovery is back and now there is just hope that it continues on an upward path.

The best news from this month's data is that the index of favorable factors is at the highest point reached in the last year—62.7. This comes on top of a rise to 60.7 from 59 in April. "The biggest jump took place in sales, with the reading now heading toward the 70 mark," said NACM Economist Chris Kuehl, PhD. "The factor sits at 65.6 and that is by far the highest reading notched in well over three years." Dollar collections jumped over the 60 barrier and now sits at 61.2, the highest mark in well over two years. Amount of credit extended also jumped considerably and now sits at 65—just shy of where it was at the very start of the year. "There may be fewer applications, but there are more companies seeking larger amounts of credit," Kuehl said. New credit applications fell from 59.3 to 58.9, making it the only favorable factor that's not in the 60s and that didn't increase from the month before. "The data seem to show that applications have slowed down a little, but there were slightly fewer rejections which may suggest that those applying for credit are in better financial shape and therefore somewhat fewer in number and perhaps more cautious about taking on more debt," Kuehl added.

There was relatively good news on the unfavorable factor front as well, just not as dramatic as in the favorable factors. The index remained unchanged from April, at 52.8. Rejections of credit applications improved from 52.3 to 52.7, and as pointed out above, this likely reflects fewer applications but they're coming from better credit risks. Accounts placed for collection improved as well, going from 51.7 to 53.8, which is a solid leap suggesting fewer customers are in credit crisis. Dollar amount beyond terms improved from 50 to 51.5 and there was similar trending in dollar amount of customer deductions, which moved from 50.3 to 50.4. This is positive movement, but still on the low side of the 50s. Filings for bankruptcies similarly improved, rising from 58.1 to 58.4. The only factor to fall was disputes, which deteriorated sharply from 54.7 to 50.2, which is perplexing. "It may indicate that there is a stronger desire to adjust credit arrangements as companies anticipate a period of better growth," Kuehl noted. "It may also reflect the impact of the first quarter slump and the temporary nature of that economic dip."

Though there was no movement in the unfavorable factor index, at least all the numbers are above 50. "The impact of the bad first quarter is still being felt and it may be another month or two before the rebound noted in the favorable categories starts to make a real dent in the unfavorable categories," Kuehl said. "The news is good in the right places and there are fewer warning signs or cautionary notes this month. If that trend can be sustained for a few more months, one can talk of real recovery by the middle of the year, but thus far it seems that one good month is often followed by a more challenging one."

Combined Manufacturing and Service Sectors (seasonally adjusted)	May '13	Jun '13	Jul '13	Aug '13	Sep '13	Oct '13	Nov '13	Dec '13	Jan '14	Feb '14	Mar '14	Apr '14	May '14
Sales	63.0	62.3	61.4	63.1	62.7	62.5	63.4	58.7	61.5	59.4	59.1	61.8	65.6
New credit applications	59.2	58.8	58.0	58.7	57.4	58.5	59.2	57.2	58.2	58.1	57.3	59.3	58.9
Dollar collections	59.2	59.3	57.5	60.4	60.6	61.4	59.7	58.7	60.9	58.8	56.4	58.1	61.2
Amount of credit extended	65.0	62.8	62.4	63.3	62.9	63.8	63.2	62.6	65.4	61.4	63.1	63.8	65.0
Index of favorable factors	**61.6**	**60.8**	**59.8**	**61.4**	**60.9**	**61.5**	**61.3**	**59.3**	**61.5**	**59.4**	**59.0**	**60.7**	**62.7**
Rejections of credit applications	50.8	52.5	53.2	52.7	53.0	52.1	53.3	54.5	54.6	52.3	52.4	52.3	52.7
Accounts placed for collection	50.6	53.9	53.6	52.5	54.3	53.3	55.0	53.4	55.2	54.6	54.1	51.7	53.8
Disputes	48.5	51.9	51.0	51.6	51.7	51.8	51.9	50.7	52.2	51.9	50.9	54.7	50.2
Dollar amount beyond terms	54.1	50.5	48.5	51.1	52.2	52.7	54.7	49.7	52.8	51.1	52.4	50.0	51.5
Dollar amount of customer deductions	49.6	52.5	51.0	51.4	51.7	51.8	52.4	51.5	51.6	50.4	51.2	50.3	50.4
Filings for bankruptcies	56.0	56.8	58.2	58.7	59.8	59.6	59.0	59.0	60.5	58.5	58.4	58.1	58.4
Index of unfavorable factors	**51.6**	**53.0**	**52.6**	**53.0**	**53.8**	**53.6**	**54.3**	**53.1**	**54.5**	**53.1**	**53.2**	**52.8**	**52.8**
NACM Combined CMI	**55.6**	**56.1**	**55.5**	**56.4**	**56.6**	**56.7**	**57.1**	**55.6**	**57.3**	**55.6**	**55.5**	**56.0**	**56.8**



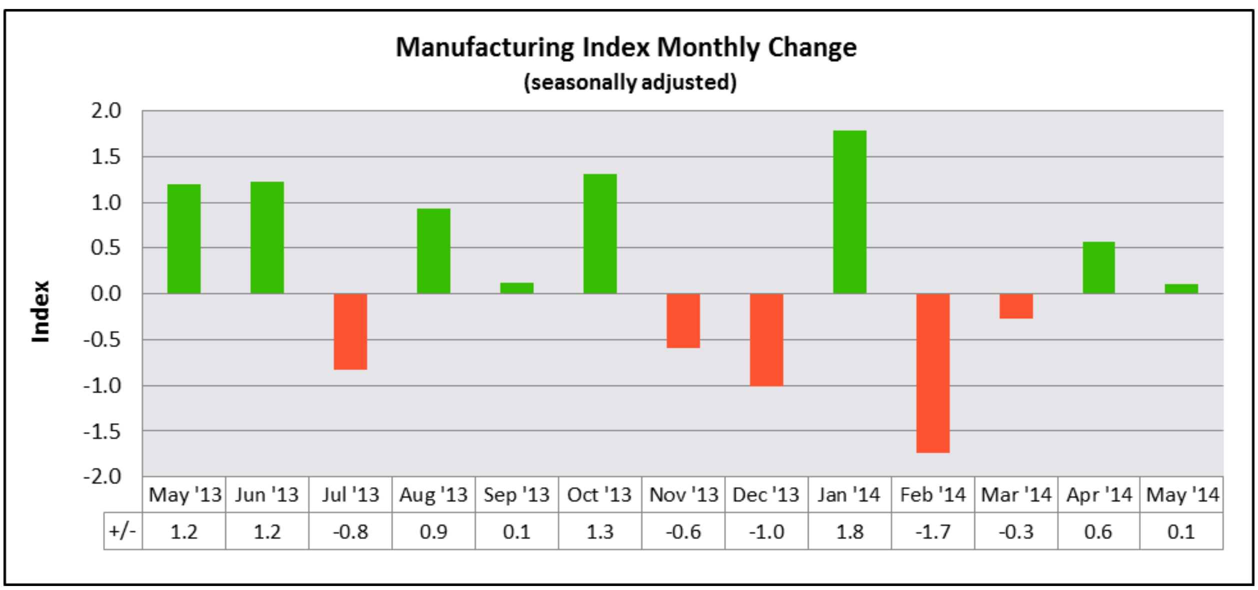
Manufacturing Sector

The manufacturing index nudged up to 56.1, a tepid gain compared to the service sector. However, it is maintaining a period of expansion only partly interrupted by the slump at the start of the year due to the cold and snow. It is predicted that it will take most of this quarter to get back on track.

Better news appeared in the manufacturing favorable factor index, which improved from 61 to 62. The jump in sales from 61.6 to 64.5 took the reading to its highest point in well over two years. "The evidence suggests that much of this gain manifested in the industries that had slumped at the start of the year, especially those oriented toward exporting," Kuehl said. Dollar collections also improved, from 59.1 to 62.0, while the other two favorable factors fell; new credit applications slipped from 58.8 to 57.2, seemingly reflecting a greater degree of caution in acquiring credit, and amount of credit extended dipped slightly from 64.5 to 64.4. "The lingering impact of the winter blast is felt in these manufacturing numbers," Kuehl said. "The sense is that improved performance will be noted in the coming months, but that depends on whether there are more shocks to come."

The unfavorable factors deteriorated to 52.2 from the 52.7 recorded in April due to disputes, which dropped sharply from 57.2 to 49.6—the factor's first time in contraction territory since last August. It is a mystery as to why it rose. Rejections of credit applications stayed at 52.6, comfortably above the 50 mark that denotes expansion but lacking the more impressive expansion of only a few months ago. Accounts placed for collection made a better than expected improvement from 51.5 to 53.3, showing fewer struggling companies than many thought there might be after the rough first quarter. Dollar amount beyond terms left contraction behind by improving from 49.5 to 52.5. "This is good news for those concerned about the growth of the late and slow payers," Kuehl said. Filings for bankruptcies also improved very slightly from 57 to 57.1. The only other factor to fall was dollar amount of customer deductions, from 48.5 to 48.3. "This marks the sixth time in the last 12 months it has been under 50 and is a trend that needs to reverse soon if there is going to be a solid rebound in the overall economy," Kuehl said. "The bottom line for the unfavorable categories is that first quarter struggles are still affecting the manufacturing sector and it appears that these troubles will be playing a role for a while longer."

Manufacturing Sector (seasonally adjusted)	May '13	Jun '13	Jul '13	Aug '13	Sep '13	Oct '13	Nov '13	Dec '13	Jan '14	Feb '14	Mar '14	Apr '14	May '14
Sales	59.2	61.0	60.3	62.3	61.6	64.3	63.4	61.7	59.6	57.9	58.5	61.6	64.5
New credit applications	57.4	58.6	57.5	58.4	55.6	58.9	59.2	57.7	59.5	57.7	56.1	58.8	57.2
Dollar collections	58.5	59.4	57.9	61.0	60.5	61.4	58.7	59.5	62.7	56.4	57.4	59.1	62.0
Amount of credit extended	63.3	61.2	61.4	62.1	62.4	64.8	61.8	61.5	66.4	60.4	61.7	64.5	64.4
Index of favorable factors	**59.6**	**60.0**	**59.3**	**61.0**	**60.0**	**62.4**	**60.8**	**60.1**	**62.0**	**58.1**	**58.4**	**61.0**	**62.0**
Rejections of credit applications	51.3	52.7	52.9	52.3	52.4	52.0	52.9	55.5	54.4	52.8	52.6	52.6	52.6
Accounts placed for collection	50.3	53.6	53.6	53.0	53.7	54.0	55.7	53.3	55.7	59.9	56.1	51.5	53.3
Disputes	46.8	50.8	49.5	49.8	50.8	52.1	51	50.2	51.0	51.6	50.6	57.2	49.6
Dollar amount beyond terms	55.7	50.8	48.3	52.5	52.9	54.6	54.8	50.0	53.2	51.7	52.8	49.5	52.5
Dollar amount of customer deductions	48.2	52.5	49.8	49.3	50.7	51.9	51.4	49.7	51.8	50.4	50.4	48.5	48.3
Filings for bankruptcies	54.7	57.1	58.1	57.9	59.4	59.0	58.5	57.7	60.4	58.6	58.5	57.0	57.1
Index of unfavorable factors	**51.1**	**52.9**	**52.0**	**52.5**	**53.3**	**53.9**	**54**	**52.7**	**54.4**	**54.1**	**53.5**	**52.7**	**52.2**
NACM Manufacturing CMI	**54.5**	**55.8**	**54.9**	**55.9**	**56.0**	**57.3**	**56.7**	**55.7**	**57.5**	**55.7**	**55.5**	**56.0**	**56.1**



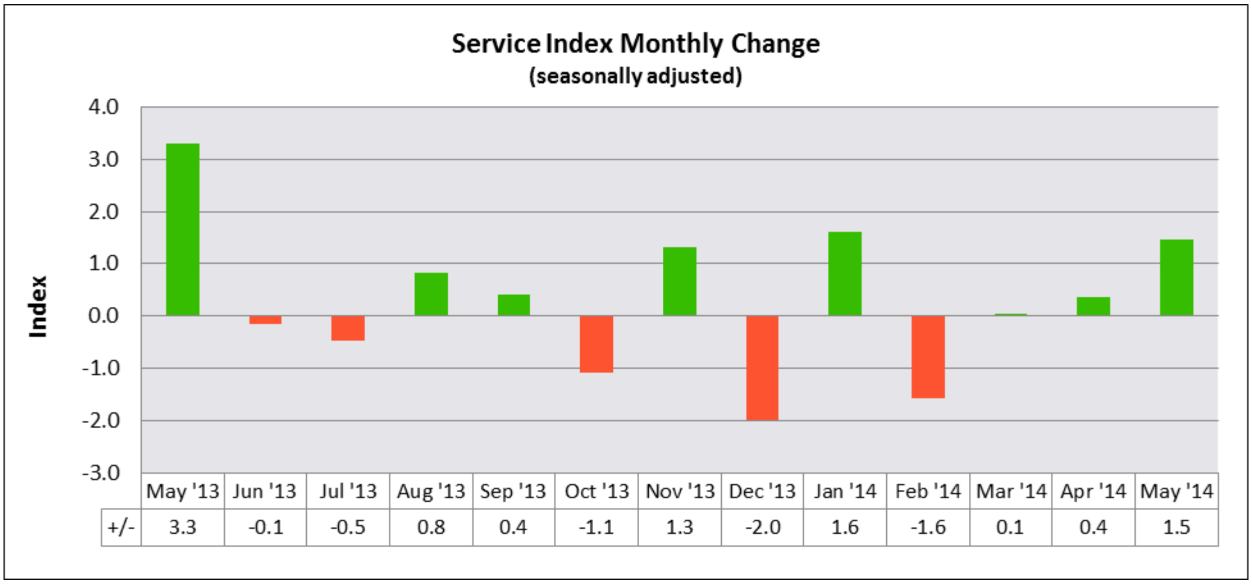
Service Sector

"The service sector brings most of the good news for the CMI this month," said Kuehl. "The sector is more diverse than manufacturing, as it includes everything from retail to construction to health care. The dominant categories are retail and construction, but the others can play a role as well. The overall number improved from 56 to 57.4, marking the highest reading since November. This is worth a pause as this means that retail is performing about as well as it was in the middle of the holiday spending season."

The most significant jumps occurred in the favorable factors. The largest surge appeared in sales, from 61.9 to 66.6. "This is a very impressive boost as it reflects a surge in retail activity that was anticipated but nobody knew to what extent, and the reading is as robust as any seen since last May when it reached 66.7," said Kuehl. New credit applications went from 59.8 to 60.7, dollar collections rose from 57.1 to 60.5 and amount of credit extended improved from 63.1 to 65.7. "All factors are above 60, the first time since the recession started in 2009," said Kuehl. "Granted some categories are right on the edge, but this is still pretty encouraging news. The level of consumer confidence has also improved of late and that bodes well for the rest of the year."

The behavior of the unfavorable factors improved as well. The index improved from 53 to 53.4. The gains were not as impressive as in the favorable factor index, but there are still some surprises given that winter really slowed the progress of the retail sector. Rejections of credit applications improved from 51.9 to 52.8, as did accounts placed for collection, from 51.8 to 54.4, dollar amount of customer deductions, from 52.1 to 52.4, and filings for bankruptcies, from 59.2 to 59.8. "The good news regarding bankruptcies is that two of the more sensitive areas in the economy are not getting hit as hard as they might have," said Kuehl. "The rate has been traditionally higher in retail and construction, but neither seems to be in serious distress right at the moment." A couple of factors, disputes and dollar amount beyond terms, slipped. The 52.1 to 50.8 slip in disputes, as with the manufacturing sector, is somewhat confusing. The dollar amount beyond terms performance was essentially flat, falling from 50.5 to 50.4.

Service Sector **(seasonally adjusted)**	**May '13**	**Jun '13**	**Jul '13**	**Aug '13**	**Sep '13**	**Oct '13**	**Nov '13**	**Dec '13**	**Jan '14**	**Feb '14**	**Mar '14**	**Apr '14**	**May '14**
Sales	66.7	63.6	62.5	63.9	63.8	60.6	63.4	55.7	63.4	60.9	59.6	61.9	66.6
New credit applications	61.0	59.1	58.4	59.1	59.2	58.1	59.1	56.7	57.0	58.5	58.5	59.8	60.7
Dollar collections	59.9	59.3	57.1	59.8	60.7	61.3	60.6	57.8	59.2	61.1	55.4	57.1	60.5
Amount of credit extended	66.8	64.3	63.3	64.5	63.4	62.8	64.5	63.6	64.4	62.3	64.5	63.1	65.7
Index of favorable factors	**63.6**	**61.6**	**60.3**	**61.8**	**61.8**	**60.7**	**61.9**	**58.4**	**61.0**	**60.7**	**59.5**	**60.5**	**63.4**
Rejections of credit applications	50.2	52.4	53.5	53.2	53.7	52.2	53.6	53.5	54.8	51.8	52.2	51.9	52.8
Accounts placed for collection	51.0	54.1	53.6	52.0	55.0	52.7	54.2	53.5	54.8	49.3	52.2	51.8	54.4
Disputes	50.2	53.0	52.6	53.3	52.6	51.4	52.8	51.3	53.3	52.2	51.2	52.1	50.8
Dollar amount beyond terms	52.5	50.3	48.7	49.7	51.5	50.9	54.5	49.3	52.3	50.6	52.0	50.5	50.4
Dollar amount of customer deductions	51.0	52.5	52.2	53.5	52.8	51.8	53.3	53.3	51.4	50.4	51.9	52.1	52.4
Filings for bankruptcies	57.2	56.5	58.2	59.6	60.1	60.3	59.4	60.4	60.5	58.4	58.4	59.2	59.8
Index of unfavorable factors	**52.0**	**53.1**	**53.1**	**53.6**	**54.3**	**53.2**	**54.6**	**53.6**	**54.5**	**52.1**	**53.0**	**53.0**	**53.4**
NACM Service CMI	**56.6**	**56.5**	**56.0**	**56.9**	**57.3**	**56.2**	**57.5**	**55.5**	**57.1**	**55.5**	**55.6**	**56.0**	**57.4**



May 2014 versus May 2013

"The trend is good for a change and right now the service sector seems to be playing the leading role," said Kuehl. "It is showing solid gains, enough to propel the entire index forward, and that suggests better days ahead now that the winter doldrums are well and truly in the past."

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 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 the PMI and other manufacturing and service sector indices.

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 15,000 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, education, products and services designed to improve the management of business credit and accounts receivable. NACM's collective voice has influenced our nation's policy makers on federal legislation concerning commercial business and trade credit for more than 100 years, and continues to play an active role in legislative issues that pertain 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.

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