Report for May 2012

Issued May 31, 2012

National Association of Credit Management

Combined Sectors

It can now be said that the economy has experienced a third straight year of "spring swoon." In 2010 this was provoked by a premature recovery that made the first quarter look stronger than it really was, and the 2011 culprits seemed to be the supply chain disruption from the earthquake in Japan, as well as the Arab Spring's impact on oil prices. What seems to be the problem in 2012? One explanation holds that the European crisis has become this year's "black swan" as it has affected everything from banks to exports. A second opinion contends there is nothing really wrong with the economic recovery, but that industry is just taking a breather. A third holds that the consumer is hibernating again as they react to everything from high jobless numbers to inflation.

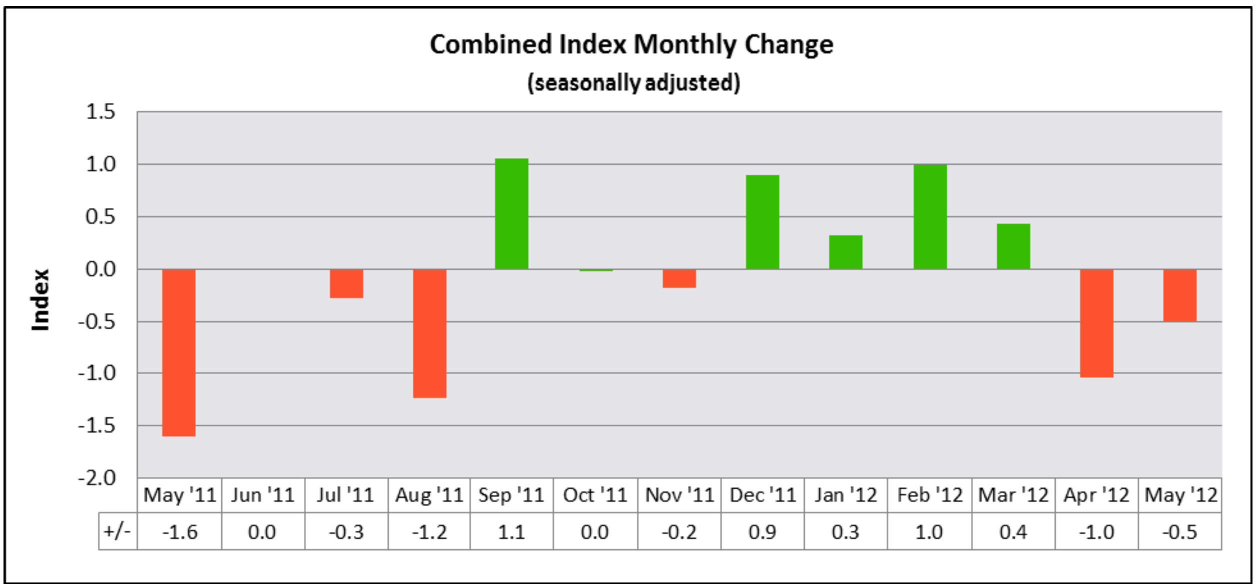
The latest Credit Managers' Index lends some support to all three scenarios, but mostly the data underpins the sense that consumers are in retreat. This is not necessarily bad news, as the consumer can come back to life under the right conditions. The overall CMI slipped again in May and is now sitting at levels last seen in January of this year and about where the CMI was a year ago. "The gains made in the last year have largely been erased and now the question is whether there will be a swift and significant comeback," said NACM Economist Chris Kuehl, PhD. "The drop from 55.1 in April to 54.6 in May is not quite as steep as the one from 56.2 in March to 55.1 in April, but the decline is worrisome nonetheless."

If there are silver linings in this month's report it is that favorable factors did not change much—the favorable index retreated from 60.5 to 60.2. Sales data actually improved from 60 to 61.2, but remains off the pace set earlier in the year when sales hit 64.4. Even better news came from new credit applications, which rose from 58.2 to 59.9. The retreat, and the bad news, was due largely to the decline in the amount of credit extended—down from 64.6 to 61.3. Part of that decline can be attributed to less credit being requested, and more of those asking for credit being denied.

May's data indicated more turmoil in the index of unfavorable factors compared to April's slight shift, said Kuehl. "As suggested last month, the majority of the business community lacks the flexibility to handle many weeks of downturn before there are problems, and this month's unfavorable factors show that this is the case," he noted. Dollar amount beyond terms fell into contraction territory from 50 to 48, as did disputes, which fell from 50.7 to 49.4. Most factor numbers dropped a little, but a big change in dollars beyond terms often signals more issues to come. In the end, the total index of unfavorable factors slid from 51.6 to 50.9. This is not catastrophic, as this is close to where the readings have been for the past year, but there had been hope of some serious recovery gains by this point, not a reversal. At 50.9, the unfavorable factor index is less than a point from sliding into contraction territory—a place the index has managed to avoid since October 2011.

"The sense of the index for this month is that nothing has developed to perk the economy up, but neither is there evidence of an imminent crash," said Kuehl. "The gains made in the first few months have proven to be more ephemeral than expected and many have concluded that 2012 will not break the 'spring swoon' pattern. The next challenge is to determine if this will be a long and difficult summer as in both 2011 and 2010. Nobody seems quite ready to make that declaration just yet."

Combined Manufacturing and Service Sectors (seasonally adjusted)	May '11	Jun '11	Jul '11	Aug '11	Sep '11	Oct '11	Nov '11	Dec '11	Jan '12	Feb '12	Mar '12	Apr '12	May '12
Sales	59.4	60.8	60.0	59.2	61.4	60.4	58.3	60.5	63.5	64.4	64.1	60.0	61.2
New credit applications	58.2	56.7	57.3	55.8	57.8	58.9	57.6	55.3	61.9	59.5	60.4	58.2	59.9
Dollar collections	58.7	58.1	56.2	56.9	57.8	56.8	56.9	61.4	56.8	63.0	61.4	59.3	58.5
Amount of credit extended	62.1	60.4	62.0	60.7	62.8	61.9	62.4	64.7	63.3	64.3	63.9	64.6	61.3
Index of favorable factors	**59.6**	**59.0**	**58.9**	**58.1**	**59.9**	**59.5**	**58.8**	**60.5**	**61.4**	**62.8**	**62.5**	**60.5**	**60.2**
Rejections of credit applications	51.5	50.9	51.0	50.2	49.9	50.2	49.5	49.5	50.2	50.5	50.6	51.6	51.1
Accounts placed for collection	50.3	49.8	49.9	47.6	48.7	50.1	49.5	50.0	49.1	50.9	52.0	50.3	50.5
Disputes	48.8	49.3	50.0	48.7	47.6	49.0	47.9	49.2	49.2	49.7	50.9	50.7	49.4
Dollar amount beyond terms	46.5	49.9	48.3	44.2	49.1	47.6	48.0	48.8	48.0	51.2	50.7	50.0	48.0
Dollar amount of customer deductions	48.6	50.0	48.9	49.1	49.2	48.7	48.9	49.1	50.1	48.5	51.1	50.4	50.2
Filings for bankruptcies	58.1	56.5	55.8	54.5	53.2	53.8	56.7	56.0	55.5	55.7	56.8	56.2	56.4
Index of unfavorable factors	**50.6**	**51.0**	**50.6**	**49.1**	**49.6**	**49.9**	**50.1**	**50.4**	**50.3**	**51.1**	**52.0**	**51.6**	**50.9**
NACM Combined CMI	**54.2**	**54.2**	**53.9**	**52.7**	**53.8**	**53.7**	**53.5**	**54.4**	**54.8**	**55.8**	**56.2**	**55.1**	**54.6**



Manufacturing Sector

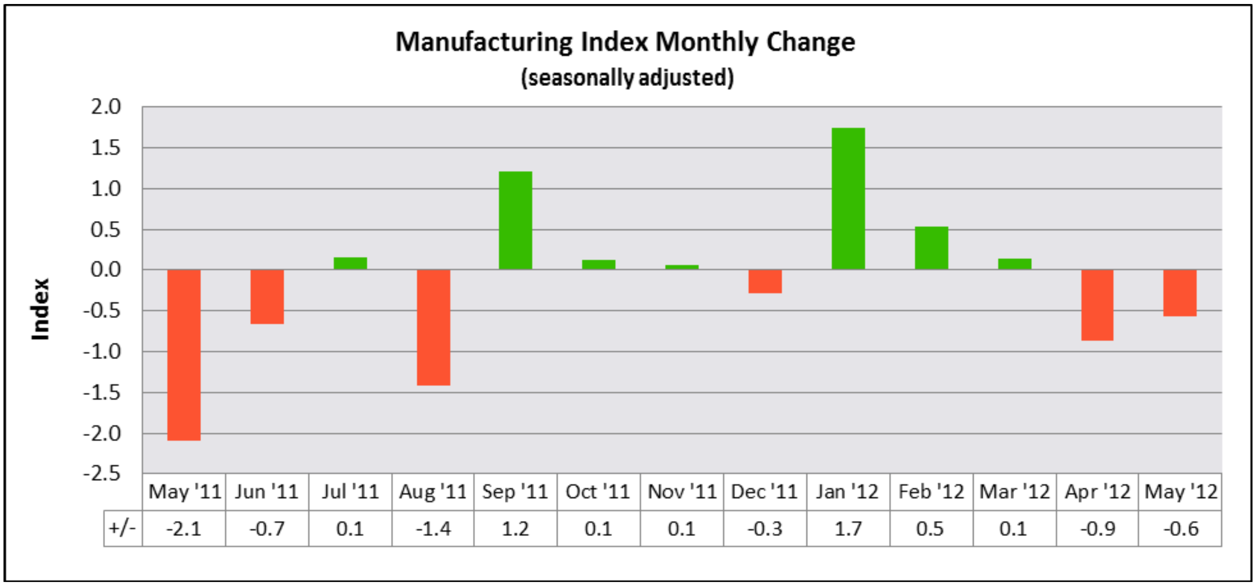
The manufacturing sector continues to bask in the glory of an election year. Regardless of what the economic issue may be, manufacturers are holding the key. Need more jobs? Turn to the manufacturers. Need to boost the export numbers? Manufacturers to the rescue. Need to find some way to extend the American Dream to the next generation, especially those who are not pursuing a college degree? It's the manufacturers. Unfortunately the sector is not up to such all-encompassing tasks. The latest data from the CMI is not bad, but the surge that many had hoped to see has not yet manifested. The good news is to be found in the index of favorable factors, but there is some offsetting bad news in the index of unfavorable factors.

Overall the manufacturing index stayed very similar to the readings from last month—moving from 54.7 to 54.2—but the really interesting material is in the sub-index readings. The index of favorable factors jumped a full point from April's reading of 59.9 to May's 60.9, led by sales, which improved from 59.4 to 61. This is not as robust as sales readings at the start of the year, but is better than a year ago, and getting back into the 60s is nothing to be dismissed. New credit applications also improved, boding well for the future. The rise from 56.6 to 61.1 marks the first time that this number has been over 60 since the anomalous month of October 2011. The only factor that declined was amount of credit extended, and it appears that part of the problem is fewer companies seeking credit with the slowing of the economy. The shift was pretty significant and took the index from 64.3 to 61. Overall, there remains some optimism in the manufacturing community and that coincides with other manufacturing data coming from the Purchasing Managers Index, as well as reports distributed by Federal Reserve banks in the New York region as well as the Midwest.

The picture is not as cheery in the unfavorable factors. The most significant and distressing reading is that the unfavorable factor index slipped under 50, the mark separating contraction from expansion, and that takes conditions back to what they were at the beginning of the year when this index stood at 49.7. The reason for the slip is many manufacturers have been investing pretty heavily in the future, leaving them with far less resiliency than would be preferred. At the beginning of the year, it looked like the economy was starting to perk up, provoking many companies to start building inventories in anticipation of demand. There was also an increase in capital investing toward the end of last year, as businesses anticipated the expiration of tax breaks for that kind of purchasing. Now that all that spending has taken place, manufacturers need the demand to justify those decisions, and the slowing economy has now put some of them in a bind.

The biggest changes in the unfavorable factor index were in disputes, dollar amount beyond terms and filings for bankruptcies. This latter indicator is of significant concern. The latest downturn has only been over the last couple of months, but that has been enough to put some manufacturers in almost instant distress. Last month, only two of the six factors were in contraction. This month saw a reversal, only two are now in expansion territory, and both are hanging onto that designation by a thread. The rejections of credit applications number is sitting at 50.4 and filings for bankruptcies is at 54.3. That latter number would be more encouraging if it were not for the fact that it stood at 56.5 only last month.

Manufacturing Sector (seasonally adjusted)	May '11	Jun '11	Jul '11	Aug '11	Sep '11	Oct '11	Nov '11	Dec '11	Jan '12	Feb '12	Mar '12	Apr '12	May '12
Sales	57.8	58.5	59.3	58.0	59.5	59.3	58.1	57.7	64.1	65.1	65.4	59.4	61.6
New credit applications	58.7	54.5	56.4	55.3	57.5	60.6	55.7	49.5	64.2	59.3	57.9	56.6	61.1
Dollar collections	60.1	55.3	55.4	56.0	56.7	56.5	56.2	58.0	56.8	61.4	62.2	59.2	59.7
Amount of credit extended	61.4	59.2	61.2	59.5	62.1	60.7	62.7	63.6	66.2	65.7	63.2	64.3	61.0
Index of favorable factors	**59.5**	**56.9**	**58.1**	**57.2**	**58.9**	**59.3**	**58.2**	**57.2**	**62.8**	**62.9**	**62.2**	**59.9**	**60.9**
Rejections of credit applications	52.6	51.8	50.8	50.4	50.0	49.6	49.6	49.8	50.5	50.1	49.6	51.5	50.4
Accounts placed for collection	50.7	49.8	49.4	47.3	49.6	48.8	51.6	50.7	48.6	51.1	51.6	49.9	49.0
Disputes	49.2	49.0	50.0	48.6	44.9	47.7	48.5	49.3	48.3	49.6	50.2	50.2	48.2
Dollar amount beyond terms	45.8	50.6	49.1	42.6	51.3	49.7	47.1	48.4	47.6	52.2	50.1	49.4	46.9
Dollar amount of customer deductions	47.7	49.5	47.8	48.9	48.1	47.7	48.8	49.3	49.2	46.5	50.6	50.4	49.5
Filings for bankruptcies	56.4	55.6	55.9	54.5	53.4	53.7	56.5	55.7	53.8	53.8	55.3	56.5	54.3
Index of unfavorable factors	**50.4**	**51.0**	**50.5**	**48.7**	**49.5**	**49.5**	**50.4**	**50.5**	**49.7**	**50.5**	**51.2**	**51.3**	**49.7**
NACM Manufacturing CMI	**54.0**	**53.4**	**53.5**	**52.1**	**53.3**	**53.4**	**53.5**	**53.2**	**54.9**	**55.5**	**55.6**	**54.7**	**54.2**



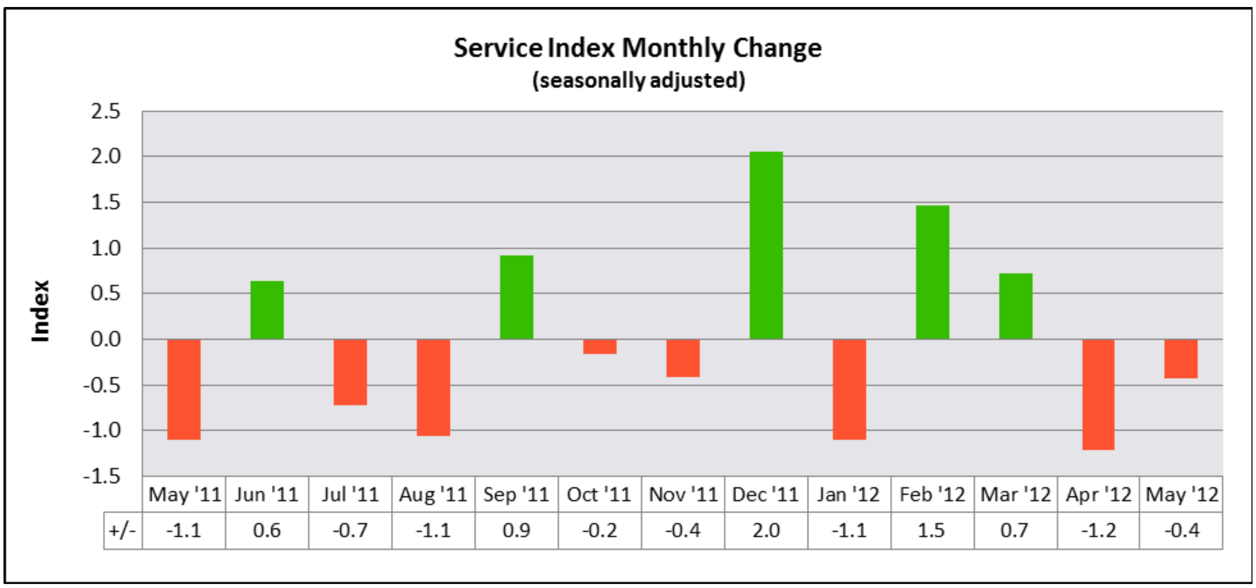
Service Sector

The overall performance of the service sector was comparable to that of the manufacturing sector, at least as far as the numbers go. Service sector index was 55.6 in April and now registers at 55.1 in May. The big difference is that there was some significant deterioration noted in the favorable factors while there was an improvement in the performance of the unfavorable factors—the mirror image of what has been taking place within the manufacturing community.

The index of favorable factors fell back into the 50s by shrinking from 61.2 to 59.6. That is the lowest reading since January and provides more ammunition to those asserting that the economy as a whole is going through yet another spring slump. It is a well-known statistic by this time, but bears repeating when so much attention is being focused on manufacturing as the engine for U.S. economic recovery. The service sector is over 80% of the U.S. economy and accounts for over 80% of all the employment in the United States. The health of this sector is critical. The good news is that sales have held steady, but the bad news is that this is the only category that improved. New credit applications slipped from 59.9 to 58.8, and dollar collections went from 59.4 to 57.3, a pretty steep decline. The amount of credit extended slid from 64.9 to 61.5, which is consistent with the slide that affected manufacturing. The fact is that credit has slowed again, both on the trade credit side, as well as from banks and other lenders.

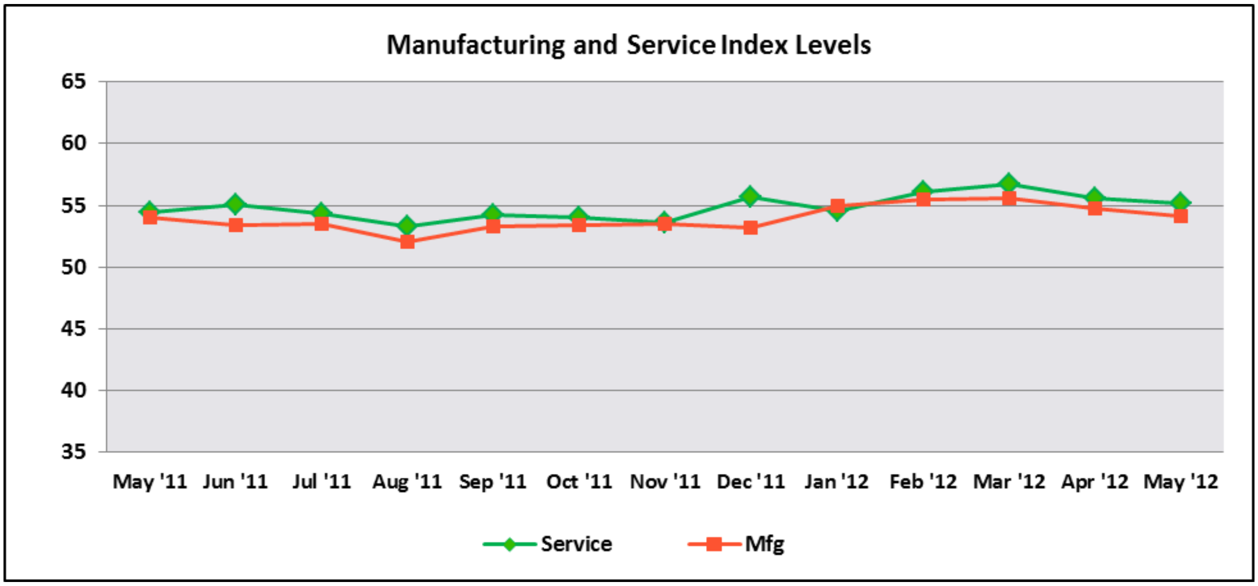
The good news is to be found in the unfavorable factor index, as it seems business in the service sector has proven to be more resilient than in manufacturing. The index actually improved from 51.8 to 52.1. In contrast to the manufacturing sector index, only one factor is under 50 and the news on bankruptcies can only be construed as good, as that number moved from 55.9 to 58.4. This suggests that the service sector has been in a better position to ride out the slowdown, and this is probably due to the limited investment in capital goods. For the most part, the categories remained very close to what they were in the previous month, or experienced very slight declines. One of the other areas of improvement was in accounts placed for collection, which went from 50.7 to 52—a very positive sign for the future. If these businesses can remain in decent shape, they will be well positioned for a resumption of recovery in the months to come. If one looks back a year, the numbers were deteriorating by this point and that heralded a summer of financial reversal.

Service Sector (seasonally adjusted)	**May '11**	**Jun '11**	**Jul '11**	**Aug '11**	**Sep '11**	**Oct '11**	**Nov '11**	**Dec '11**	**Jan '12**	**Feb '12**	**Mar '12**	**Apr '12**	**May '12**
Sales	61.1	63.2	60.7	60.5	63.3	61.5	58.4	63.3	62.9	63.6	62.8	60.6	60.9
New credit applications	57.8	58.8	58.2	56.3	58.0	57.2	59.4	61.1	59.6	59.6	62.8	59.9	58.8
Dollar collections	57.3	60.9	57.1	57.9	58.9	57.0	57.6	64.9	56.7	64.5	60.7	59.4	57.3
Amount of credit extended	62.7	61.6	62.7	61.9	63.5	63.2	62.1	65.7	60.4	63.0	64.6	64.9	61.5
Index of favorable factors	**59.7**	**61.1**	**59.7**	**59.1**	**60.9**	**59.7**	**59.4**	**63.8**	**59.9**	**62.7**	**62.7**	**61.2**	**59.6**
Rejections of credit applications	50.4	50.0	51.2	50.1	49.8	50.9	49.4	49.1	49.9	50.8	51.6	51.8	51.8
Accounts placed for collection	49.9	49.8	50.3	47.8	47.8	51.3	47.5	49.3	49.6	50.7	52.5	50.7	52.0
Disputes	48.5	49.6	50.0	48.9	50.4	50.2	47.2	49.0	50.1	49.9	51.6	51.3	50.6
Dollar amount beyond terms	47.3	49.1	47.5	45.9	46.9	45.4	48.8	49.3	48.5	50.3	51.2	50.6	49.0
Dollar amount of customer deductions	49.4	50.5	49.9	49.3	50.2	49.8	48.9	48.9	51.0	50.6	51.5	50.4	51.0
Filings for bankruptcies	59.8	57.3	55.8	54.6	53.1	54.0	57.0	56.2	57.2	57.6	58.4	55.9	58.4
Index of unfavorable factors	**50.9**	**51.0**	**50.8**	**49.4**	**49.7**	**50.3**	**49.8**	**50.3**	**51.0**	**51.6**	**52.8**	**51.8**	**52.1**
NACM Service CMI	**54.4**	**55.1**	**54.3**	**53.3**	**54.2**	**54.0**	**53.6**	**55.7**	**54.6**	**56.0**	**56.8**	**55.6**	**55.1**



May 2012 vs. May 2011

The year-to-year trend is holding right about where it has been for the past year—right along the 50 range. This is not great news by any stretch, as many had assumed there would be some improvements by now. The good news is that the news is no worse than it is.



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 900 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:

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

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.*

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 federal legislative policy 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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