Report for October 2011

Issued October 31, 2011

National Association of Credit Management

Combined Sectors

The bad news is the October Credit Managers' Index (CMI) did not see September's big gains. The good news is that there was no retreat from September's numbers. The overall index hit 53.8 in September after tumbling to 52.7 in the previous month, but in October the index essentially held steady at 53.7. There was a slight reduction in the index of favorable factors, but the index of unfavorable factors came just a little bit closer to expansion territory. The majority of economic indicators has been reasonably positive over the past few weeks and seems to be pointing to better months to come and the CMI index did not dispel this assumption, although the slower pace of progress reminds those paying attention that this is unlikely to be a rapid recovery for any but a handful of sectors.

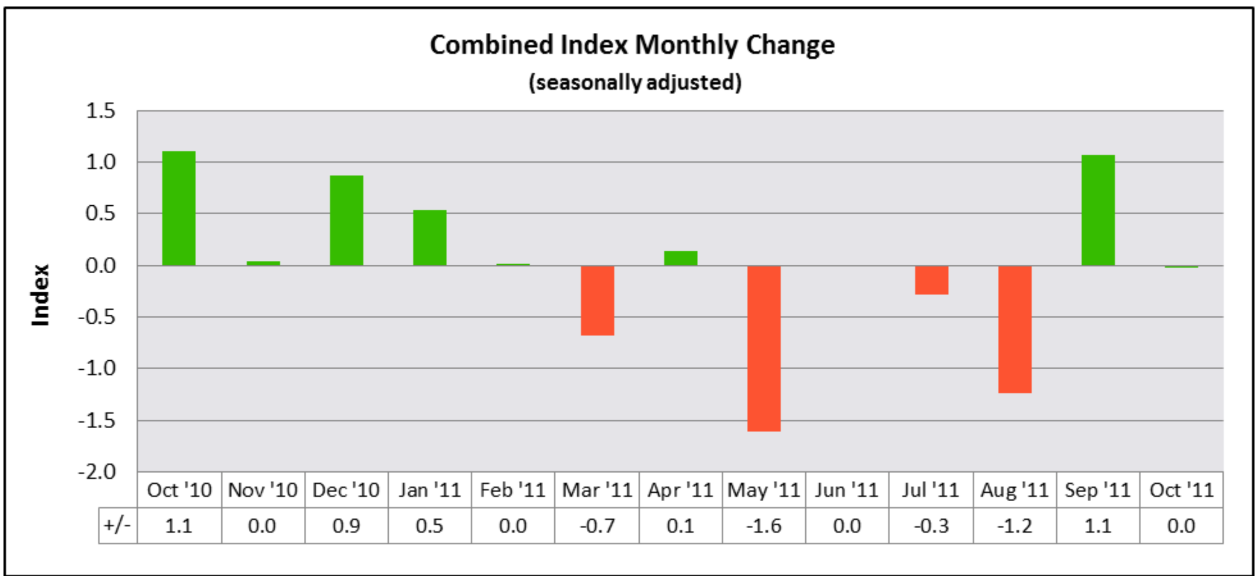
"Most of the decline took place in the favorable factors suggesting that growth is not yet ready to surge, but the fact remains that adjustments were relatively minor and remain above the trend from earlier this summer," said Chris Kuehl, PhD, economist for the National Association of Credit Management (NACM). The rate of sales slowed from the pace in September, but at 60.4 it is still higher than it has been since April. Expectations were that sales would be back to the levels set last spring, but there was evidence in the other index numbers for a slight reversal of credit availability. The number of new credit applications improved slightly to 58.9, taking this indicator back to April levels. It is apparent that more businesses are seeking to expand and are making more credit requests. The hitch is that there was a decline in the amount of credit extended. However, the decline was not dramatic, falling from 62.8 to 61.9. That leaves current readings higher than through most of the summer, but the slowdown is a bit of a concern as the holiday season begins. "It has been noted in other surveys that manufacturers are planning to spend more on capital goods than they did last year, and one of the limiting factors in that decision will be the availability of credit," said Kuehl. "Some will have an easier time clearing their financial obligations than others, although the unfavorable factor index showed solid improvement, suggesting that more companies are getting back to some measure of financial health."

Most of the positive news stemmed from the changes in unfavorable factors. These upward shifts suggest that companies are having more success getting finances in order than was the case earlier in the year. The gains in the index are starting to point to a general recovery. The pattern for the last couple of years has been separation. The weak and problematic companies for the credit manager have been fading away as bankruptcy claims them. The anecdotes from the field are nearly universal across most categories. The customers struggling to pay their bills have been slowly exiting, and those left behind are those that have seen some growth. There was a reduction in the number of credit applications rejected and that somewhat contradicts the reduction in credit issued. "The fact is that companies are asking for more credit than they may receive, but there is still evidence of credit movement," said Kuehl.

Overall, unfavorable factors showed improvement. There were fewer accounts placed for collection, fewer disputes and fewer dollars beyond terms. There were also fewer bankruptcies. The unfavorable index is still just shy of the 50 point, sitting at 49.9 and suggesting expansion over contraction, but the trend is headed in the right direction. The last time the unfavorable index was above 50 was in July and the numbers had been sinking deeper into the 40s since. The current reading is about as close to 50 as one gets and is now expected to clear that level next month.

"The latest data on the expansion of the U.S. economy in the third quarter reinforces the notion that conditions have started to improve, and the retail data thus far has been more encouraging than not," said Kuehl. "If one looks at the steady rebound in the financial stability of the business community over the last month, there is some reason to assume that conditions will improve even more in the last two months of the year."

Combined Manufacturing and Service Sectors (seasonally adjusted)	Oct '10	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct '11
Sales	60.8	61.9	65.9	63.5	66.3	64.7	64.5	59.4	60.8	60.0	59.2	61.4	60.4
New credit applications	56.8	58.2	60.1	58.6	60.3	59.8	58.8	58.2	56.7	57.3	55.8	57.8	58.9
Dollar collections	61.9	58.6	60.7	60.9	63.4	60.0	61.3	58.7	58.1	56.2	56.9	57.8	56.8
Amount of credit extended	59.8	61.2	61.7	64.8	66.5	64.4	64.7	62.1	60.4	62.0	60.7	62.8	61.9
Index of favorable factors	**59.8**	**60.0**	**62.1**	**62.0**	**64.1**	**62.2**	**62.3**	**59.6**	**59.0**	**58.9**	**58.1**	**59.9**	**59.5**
Rejections of credit applications	51.4	51.0	50.8	51.2	51.4	50.8	50.8	51.5	50.9	51.0	50.2	49.9	50.2
Accounts placed for collection	51.7	52.5	51.5	52.5	49.9	52.1	50.5	50.3	49.8	49.9	47.6	48.7	50.1
Disputes	49.9	50.8	49.2	51.0	49.2	48.9	49.3	48.8	49.3	50.0	48.7	47.6	49.0
Dollar amount beyond terms	50.9	48.9	53.4	51.5	50.6	49.7	50.7	46.5	49.9	48.3	44.2	49.1	47.6
Dollar amount of customer deductions	48.9	50.2	49.6	50.6	50.1	49.3	49.9	48.6	50.0	48.9	49.1	49.2	48.7
Filings for bankruptcies	57.0	56.3	55.4	59.1	56.0	57.4	58.1	58.1	56.5	55.8	54.5	53.2	53.8
Index of unfavorable factors	**51.6**	**51.6**	**51.7**	**52.6**	**51.2**	**51.4**	**51.5**	**50.6**	**51.0**	**50.6**	**49.1**	**49.6**	**49.9**
NACM Combined CMI	**54.9**	**55.0**	**55.8**	**56.4**	**56.4**	**55.7**	**55.8**	**54.2**	**54.2**	**53.9**	**52.7**	**53.8**	**53.7**



Manufacturing Sector

The manufacturing sector continues to gain momentum and this is reflected in both the favorable and unfavorable factors. The favorable factor index gained from 58.9 to 59.3, taking the index back to levels last seen in May. The peak in the past year was reached in February where it stood at 63.4, and now there is some expectation that the index could reach back into the 60s again before the end of the year. The cautionary note is that manufacturing in general tends to slow down a bit toward the end of the year and much will depend on whether the retailers stick to their strategy of keeping inventory levels low and settling for what they can get from the consumer without spending to replenish. If the initial sales are strong enough, there will be pressure to put more inventory in place and that could provoke a late rush for those that supply retail, but the betting is that retailers will remain cautious and will limit their urge to build back inventory.

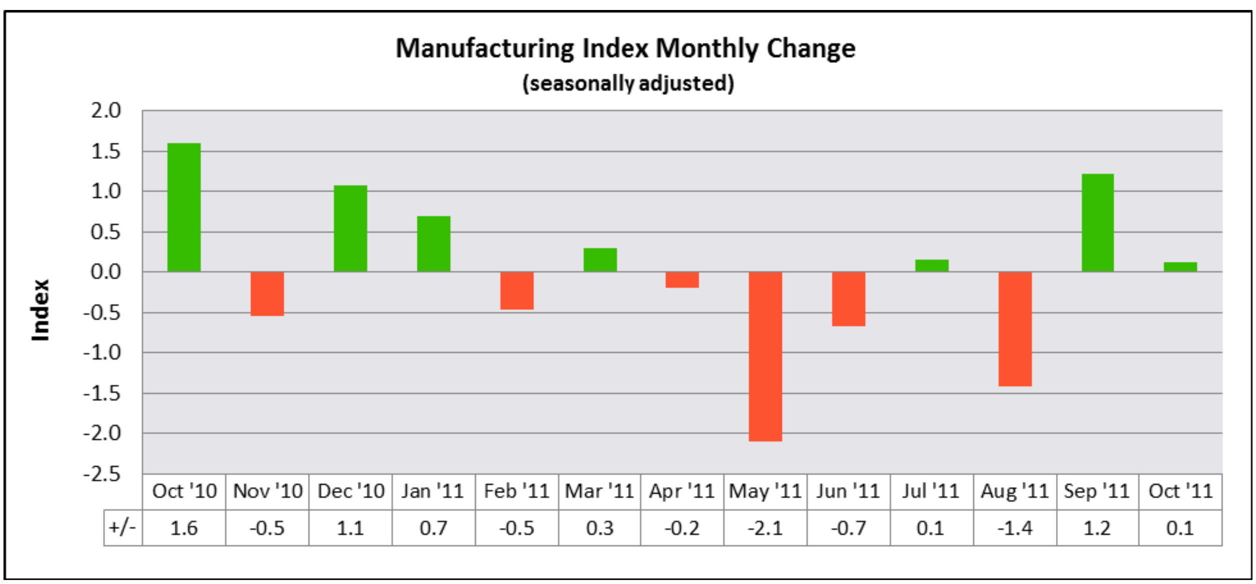
The major factor in the growth of the manufacturing side appears to be anticipation of a better 2012. The surveys on capital expenditure suggest that most are planning to make some significant capital equipment purchases and that generally triggers more credit requests. The jump from 57.5 to 60.6 in new credit applications illustrates that point.

There was a reduction in the amount of credit extended however—from 62.1 to 60.7. This seems to reflect that some of those asking for credit are not in a very strong position.

The index of unfavorable factors was unchanged from September, but there was some variance within the categories. There were more rejections of credit applications based on the same factors that limited credit. More companies sought credit despite some financial issues that serve to restrain them. In general, there were more signs of stress, but some of the more serious declines leveled off a little this month. The number of disputes declined as this indicator went from a very low point of 44.9 to a slightly better 47.7. The number of bankruptcies declined slightly as well, the index shifting from 53.4 to 53.7.

It has been observed that the manufacturing sector is still working itself out. Those companies operating in fast-growing sectors like energy and health care are doing very well and expanding. The auto sector is undergoing a recovery as well. In contrast, there are the companies connected to the construction sector, a still highly stressed part of the economy no matter what category one examines. Residential housing is not performing well at all, but neither is commercial construction. Even the public sector activity has been in decline as the arguments over what to do with infrastructure projects continue.

Manufacturing Sector (seasonally adjusted)	Oct '10	Nov	Dec '10	Jan '11	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct '11
Sales	59.3	62.2	66.6	64.7	65.1	65.4	63.9	57.8	58.5	59.3	58.0	59.5	59.3
New credit applications	54.9	57.8	59.1	57.7	59.6	60.6	60.3	58.7	54.5	56.4	55.3	57.5	60.6
Dollar collections	61.0	57.9	60.5	60.3	61.5	60.8	60.2	60.1	55.3	55.4	56.0	56.7	56.5
Amount of credit extended	59.9	61.2	61.6	66.2	67.6	64.5	66.5	61.4	59.2	61.2	59.5	62.1	60.7
Index of favorable factors	**58.8**	**59.8**	**61.9**	**62.2**	**63.4**	**62.8**	**62.7**	**59.5**	**56.9**	**58.1**	**57.2**	**58.9**	**59.3**
Rejections of credit applications	53.2	52.1	51.3	52.0	51.9	51.6	51.0	52.6	51.8	50.8	50.4	50.0	49.6
Accounts placed for collection	53.6	52.7	51.1	53.0	51.2	53.9	50.7	50.7	49.8	49.4	47.3	49.6	48.8
Disputes	49.5	48.6	48.1	49.8	48.2	49.0	50.5	49.2	49.0	50.0	48.6	44.9	47.7
Dollar amount beyond terms	55.2	49.4	53.9	52.1	51.3	51.6	52.2	45.8	50.6	49.1	42.6	51.3	49.7
Dollar amount of customer deductions	48.5	48.8	49.4	49.1	50.1	48.8	49.5	47.7	49.5	47.8	48.9	48.1	47.7
Filings for bankruptcies	57.7	56.7	56.5	60.2	53.9	57.2	56.8	56.4	55.6	55.9	54.5	53.4	53.7
Index of unfavorable factors	**52.9**	**51.4**	**51.7**	**52.7**	**51.1**	**52.0**	**51.8**	**50.4**	**51.0**	**50.5**	**48.7**	**49.5**	**49.5**
NACM Manufacturing CMI	**55.3**	**54.7**	**55.8**	**56.5**	**56.0**	**56.3**	**56.1**	**54.0**	**53.4**	**53.5**	**52.1**	**53.3**	**53.4**

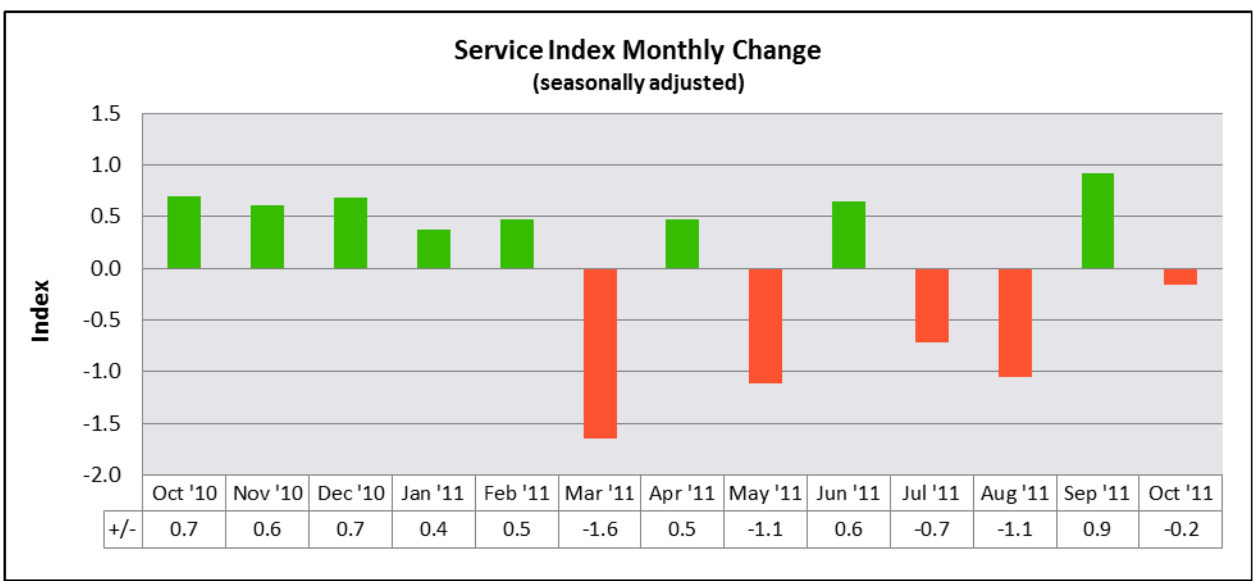


Service Sector

Service sector performance was weaker than many had expected given the decent retail performance noted in the last few months. The most startling decline was in sales, as the index slipped from 63.3 to 61.5. This is not a major inhibition given that the current reading is still in line with the progress through the last few months. There was also a decline in the number of new credit applications as they fell from 58 to 57.2. In all, the favorable factors tumbled from 60.9 to 59.7. This is not a major decline, but diminishes the overall index back to July levels, which was the worst point in the year by most accounts. The industries that seem to have brought down the overall index include construction and, to some degree, financial services while retail performed a little better than expected.

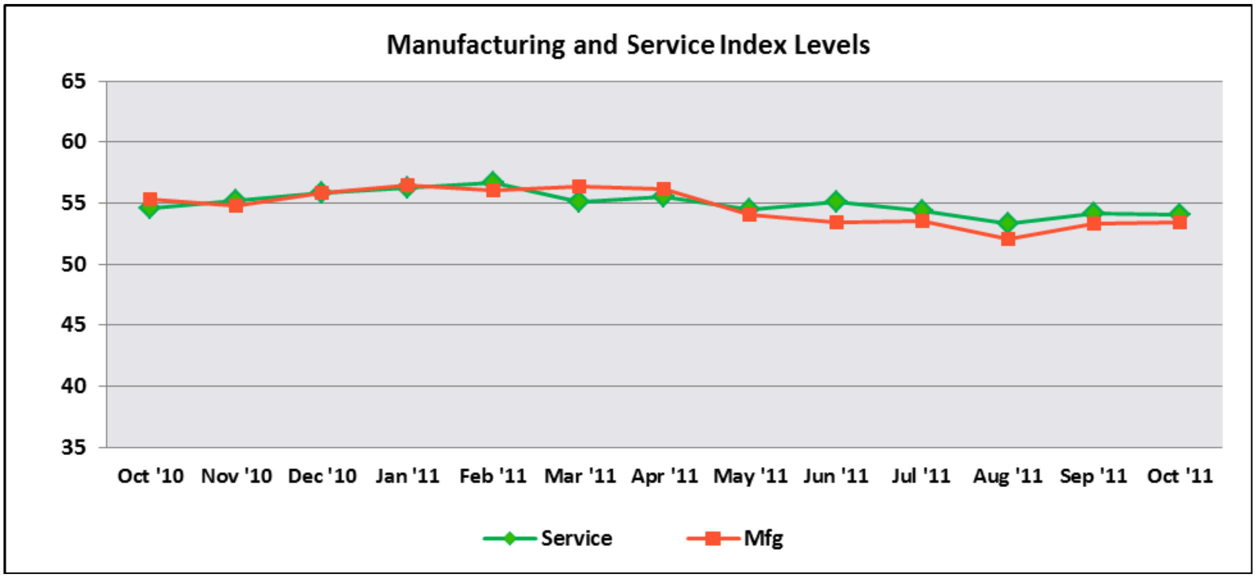
The good news was a palpable improvement in unfavorable factors. The overall index moved from 49.7 to 50.3, returning to expansion territory—albeit by a hair. The factors that led to this improvement included fewer credit applications being rejected, fewer accounts placed for collection and a significant improvement in bankruptcy filings. As with the manufacturing sector, it appears that the weakest customers are fading away and leaving the field to those that are more suited to long-term survival. This is good news for later, but in the meantime these business failures leave some holes in the books. There is likely to be more credit that is simply abandoned, as there will be little chance of collecting—at least in the short term.

Service Sector (seasonally adjusted)	**Oct '10**	**Nov**	**Dec '10**	**Jan '11**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct '11**
Sales	62.2	61.6	65.1	62.3	67.5	63.9	65.0	61.1	63.2	60.7	60.5	63.3	61.5
New credit applications	58.7	58.6	61.1	59.4	61.0	59.0	57.3	57.8	58.8	58.2	56.3	58.0	57.2
Dollar collections	62.9	59.2	60.9	61.6	65.2	59.2	62.3	57.3	60.9	57.1	57.9	58.9	57.0
Amount of credit extended	59.6	61.2	61.8	63.4	65.4	64.2	63.0	62.7	61.6	62.7	61.9	63.5	63.2
Index of favorable factors	**60.9**	**60.2**	**62.2**	**61.7**	**64.8**	**61.6**	**61.9**	**59.7**	**61.1**	**59.7**	**59.1**	**60.9**	**59.7**
Rejections of credit applications	49.6	49.8	50.3	50.4	51.0	50.1	50.5	50.4	50.0	51.2	50.1	49.8	50.9
Accounts placed for collection	49.9	52.4	52.0	52.1	48.6	50.2	50.2	49.9	49.8	50.3	47.8	47.8	51.3
Disputes	50.3	52.9	50.3	52.1	50.1	48.7	48.1	48.5	49.6	50.0	48.9	50.4	50.2
Dollar amount beyond terms	46.6	48.5	52.9	51.0	49.9	47.8	49.2	47.3	49.1	47.5	45.9	46.9	45.4
Dollar amount of customer deductions	49.4	51.6	49.9	52.1	50.1	49.8	50.3	49.4	50.5	49.9	49.3	50.2	49.8
Filings for bankruptcies	56.3	55.9	54.3	57.9	58.2	57.7	59.5	59.8	57.3	55.8	54.6	53.1	54.0
Index of unfavorable factors	**50.4**	**51.8**	**51.6**	**52.6**	**51.3**	**50.7**	**51.3**	**50.9**	**51.0**	**50.8**	**49.4**	**49.7**	**50.3**
NACM Service CMI	**54.6**	**55.2**	**55.8**	**56.2**	**56.7**	**55.1**	**55.5**	**54.4**	**55.1**	**54.3**	**53.3**	**54.2**	**54.0**



October 2011 vs. October 2010

The data suggest a steady state for the most part. The overall trend line still holds above 50, but not by much. This is still a very slow rebound and there is still a very real threat of slipping beneath the 50 line that separates expansion from contraction. The good news is that the expansion process continues, but it remains vulnerable, if not anemic.



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 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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