



Report for July 2012

Issued July 31, 2012

National Association of Credit Management

Combined Sectors

The Credit Managers' Index reflects the grim reality of the economy of summer 2012, dropping in July from 54.5 to 53.4. It became obvious in May that another spring swoon was underway, and like the last few years, the summer is becoming an extension of the deterioration. The problems besetting the economy earlier in the year have not abated, and now there are new ones emerging. Thus far it is hard to see what impact the drought will have on the greater manufacturing and service economies, but given that the farm sector helped drive manufacturing last year, the sudden drop in demand for machinery isn't welcome.

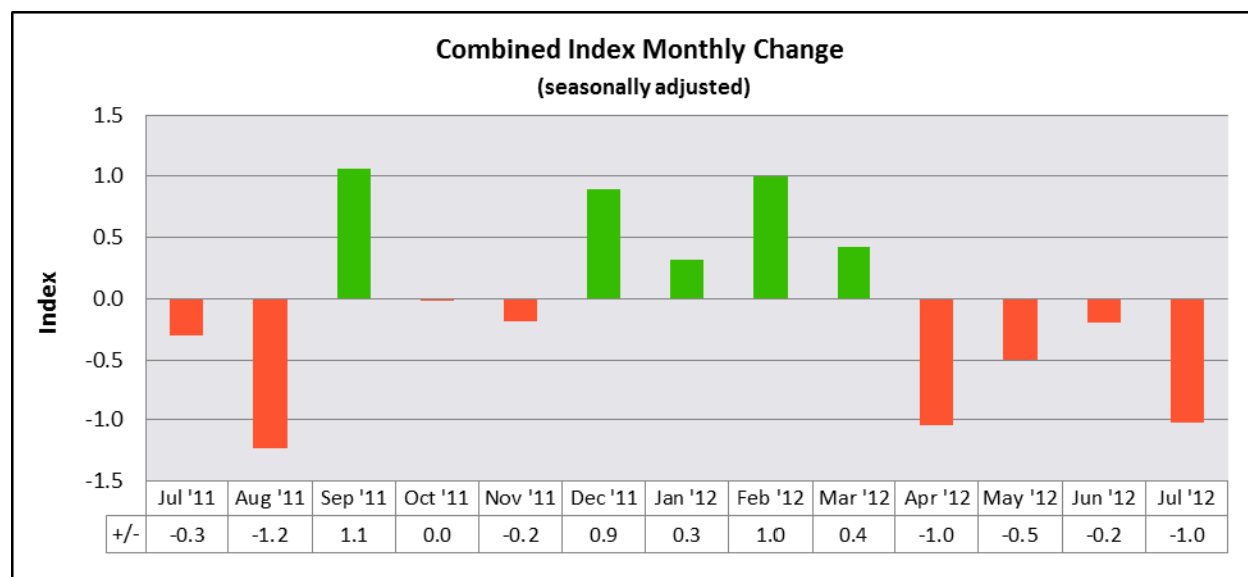
There are some signs of nascent recovery, but these have not been enough to reverse the course of the last few months. If one looks at the favorable factors that usually signal future growth, there is evidence that the slump is setting in more aggressively. For the first time in over a year, sales fell below 60, and by a significant degree. The reading of 58.5 is worse than at any point in 2011. New credit applications stabilized to some degree; June's reading was 57.5, and now it sits at 57.2. This is a long way from the 61.9 registered in January when expectations were upbeat. There was also a decline in dollar collections, from 60 to 58.7, and rounding out favorable factors with yet another decline was amount of credit extended, which slipped from 62.6 to 61.3. Altogether, the favorable factor index slid from 60.2 to 58.9, marking the first time it has fallen under 60 since November 2011. This was not what this year was supposed to look like, and when the specifics of the decline are examined, it is apparent that the real damage has been in the volatile service sector.

Unfavorable factors are not telling an upbeat story either, which is more worrisome than the slide in the favorable index. Over the last couple of months it was noted that the economy can survive a stall in growth, provided there is no further deterioration in business conditions. The good news from this period had been fewer issues for the companies that survived the first round of economic downturn. Now there is some evidence that the last few months are starting to catch up. Rejections of credit applications is showing stability at 51.4, and is better than many expected. It would appear that the companies applying for credit are the ones doing well, and approvals are not generally suspect. There was a small improvement in accounts placed for collection, but it remains under 50—improving from 48.3 to 48.9. There were more disputes than in the past, as the reading slipped deeper into the mid-40s—from 48.9 to 47.6. Dollar amount beyond terms fell under 50 again after managing to hit 50.5 in June. It now stands at 47.8, the lowest reading since September of last year. This is not trending in the right direction. Finally, dollar amount of customer deductions slipped a bit from 48.7 to 48.2 and filings for bankruptcy worsened from 56 to 54.9.

The index of unfavorable indicators has now dipped below the magic 50 line separating expansion from contraction. This is the first time the unfavorable index has been in contraction since the end of 2010. To illustrate the swift decline, only two unfavorable categories were above 50 this month. In March, all of these categories were over 50 and in the expansion zone. This is a precipitous fall, and it is unlikely that a reversal will be swift.

As the year progresses, there are more problems to contend with and these are already pulling business expansion down. Europe's continuing crisis affects the export trade. The potential for plummeting off the fiscal cliff has almost every business uneasy, and now there are the billions of dollars lost to the drought. The two sectors that had been pulling more than their own weight were manufacturing and farming.

Combined Manufacturing and Service Sectors (seasonally adjusted)	Jul '11	Aug '11	Sep '11	Oct '11	Nov '11	Dec '11	Jan '12	Feb '12	Mar '12	Apr '12	May '12	Jun '12	Jul '12
Sales	60.0	59.2	61.4	60.4	58.3	60.5	63.5	64.4	64.1	60.0	61.2	60.6	58.5
New credit applications	57.3	55.8	57.8	58.9	57.6	55.3	61.9	59.5	60.4	58.2	59.9	57.5	57.2
Dollar collections	56.2	56.9	57.8	56.8	56.9	61.4	56.8	63.0	61.4	59.3	58.5	60.0	58.7
Amount of credit extended	62.0	60.7	62.8	61.9	62.4	64.7	63.3	64.3	63.9	64.6	61.3	62.6	61.3
Index of favorable factors	58.9	58.1	59.9	59.5	58.8	60.5	61.4	62.8	62.5	60.5	60.2	60.2	58.9
Rejections of credit applications	51.0	50.2	49.9	50.2	49.5	49.5	50.2	50.5	50.6	51.6	51.1	51.4	51.4
Accounts placed for collection	49.9	47.6	48.7	50.1	49.5	50.0	49.1	50.9	52.0	50.3	50.5	48.3	48.9
Disputes	50.0	48.7	47.6	49.0	47.9	49.2	49.2	49.7	50.9	50.7	49.4	48.9	47.6
Dollar amount beyond terms	48.3	44.2	49.1	47.6	48.0	48.8	48.0	51.2	50.7	50.0	48.0	50.5	47.8
Dollar amount of customer deductions	48.9	49.1	49.2	48.7	48.9	49.1	50.1	48.5	51.1	50.4	50.2	48.7	48.2
Filings for bankruptcies	55.8	54.5	53.2	53.8	56.7	56.0	55.5	55.7	56.8	56.2	56.4	56.0	54.9
Index of unfavorable factors	50.6	49.1	49.6	49.9	50.1	50.4	50.3	51.1	52.0	51.6	50.9	50.6	49.8
NACM Combined CMI	53.9	52.7	53.8	53.7	53.5	54.4	54.8	55.8	56.2	55.1	54.6	54.5	53.4



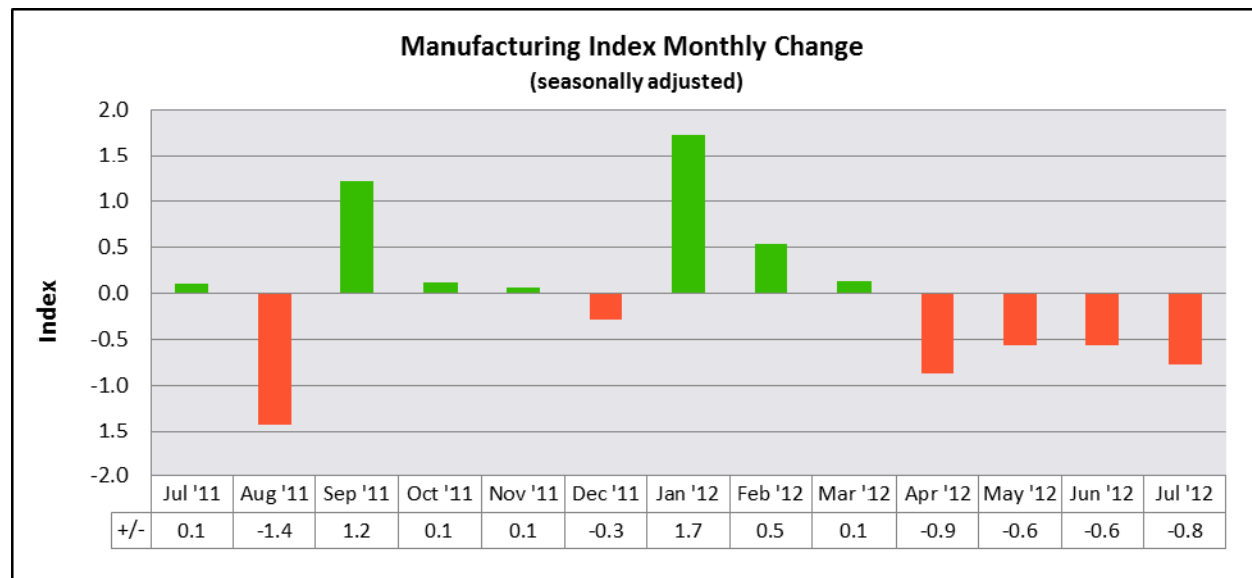
Manufacturing Sector

The data from manufacturing was not exactly promising, as the sector's index fell from 53.6 to 52.8, but it was still far less depressing than the data from the service sector. There was a decline in the favorable factor index, but the fall was not precipitous—moving from the June number of 60.4 to 58.2. This is the lowest the index has been since December, but the range thus far has been pretty narrow. The high point was in February (62.9). The sub-indices are more instructive. Sales fell from 59.1 to 57.2 and haven't been this low since early 2011. Much of this fall could be attributable to the slump in export activity. There are also clues in inventory numbers. At the first of the year, inventories were up, and that was a good thing. Now they are up again, which is not good. In January, better times ahead were expected and many companies started to build inventory in anticipation. Having inventory on hand meant less chance of bottlenecks to slow growth once it arrived. Then the economy stalled and that inventory became an anchor: material and product that could not be sold or turned into anything useful. Now manufacturers have to clear that inventory before they can get engaged in new production, delaying recovery that much more.

The other favorable factors slipped as well. New credit applications fell from 57.2 to 56.5, while dollar collections moved from 61.9 to 59.6. To round out the bad news, there was the fall from 63.2 to 59.6 for amount of credit extended. Last month, two categories were in the 60s, but they both fell into the 50s this month.

The more worrisome data comes from the index of unfavorable factors despite the improvement from 49.1 to 49.3. Rejections of credit applications increased from 50.5 to 51.2. As noted above, some self-selection appears to be taking place, as only creditworthy companies are bothering to apply. Accounts placed for collection rose from 47.7 to 49.1, which is a lot closer to expansion than last month and on a par with the reading from May. Disputes also improved from 47 to 47.6. The negative numbers came with dollar amount beyond terms, which slid to 47.8 from 49.2. This is a concern because it signals that some customers are struggling to stay current and are perhaps having cash flow issues, and these will likely not dissipate in the immediate future. Dollar amount of customer deductions remained flat, but bankruptcies worsened slightly.

Manufacturing Sector (seasonally adjusted)	Jul '11	Aug '11	Sep '11	Oct '11	Nov '11	Dec '11	Jan '12	Feb '12	Mar '12	Apr '12	May '12	Jun '12	Jul '12
Sales	59.3	58.0	59.5	59.3	58.1	57.7	64.1	65.1	65.4	59.4	61.6	59.1	57.2
New credit applications	56.4	55.3	57.5	60.6	55.7	49.5	64.2	59.3	57.9	56.6	61.1	57.2	56.5
Dollar collections	55.4	56.0	56.7	56.5	56.2	58.0	56.8	61.4	62.2	59.2	59.7	61.9	59.6
Amount of credit extended	61.2	59.5	62.1	60.7	62.7	63.6	66.2	65.7	63.2	64.3	61.0	63.2	59.6
Index of favorable factors	58.1	57.2	58.9	59.3	58.2	57.2	62.8	62.9	62.2	59.9	60.9	60.4	58.2
Rejections of credit applications	50.8	50.4	50.0	49.6	49.6	49.8	50.5	50.1	49.6	51.5	50.4	50.5	51.2
Accounts placed for collection	49.4	47.3	49.6	48.8	51.6	50.7	48.6	51.1	51.6	49.9	49.0	47.7	49.1
Disputes	50.0	48.6	44.9	47.7	48.5	49.3	48.3	49.6	50.2	50.2	48.2	47.0	47.6
Dollar amount beyond terms	49.1	42.6	51.3	49.7	47.1	48.4	47.6	52.2	50.1	49.4	46.9	49.2	47.8
Dollar amount of customer deductions	47.8	48.9	48.1	47.7	48.8	49.3	49.2	46.5	50.6	50.4	49.5	46.6	46.6
Filings for bankruptcies	55.9	54.5	53.4	53.7	56.5	55.7	53.8	53.8	55.3	56.5	54.3	53.8	53.3
Index of unfavorable factors	50.5	48.7	49.5	49.5	50.4	50.5	49.7	50.5	51.2	51.3	49.7	49.1	49.3
NACM Manufacturing CMI	53.5	52.1	53.3	53.4	53.5	53.2	54.9	55.5	55.6	54.7	54.2	53.6	52.8



Service Sector

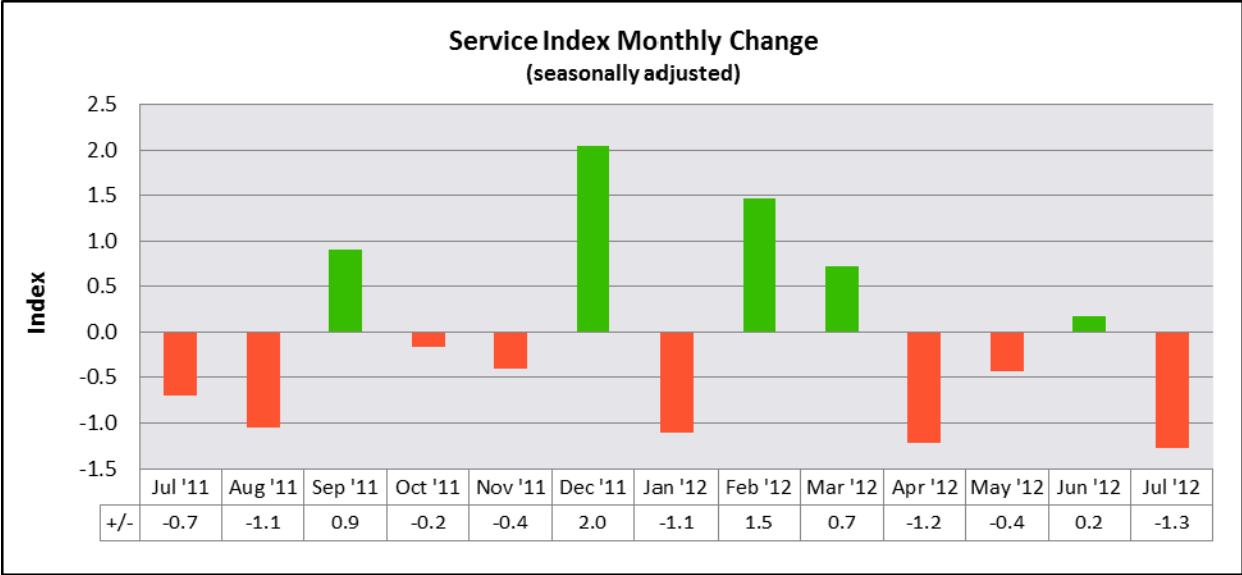
The really troubling news this month comes from the service sector. The index dropped from 55.3 to 54, the lowest reading since November 2011. Granted, the service index has not been appreciably higher than 55 for the last several months, but the slide is certainly taking the data in the wrong direction. The highest reading (56.8) was back in March.

The current sales reading is at 59.8, but the last time this index was under 60 was also in November when it slipped to 58.4. That month was seen as something of an anomaly, as the readings had been consistently in the 60s prior to that. The pace of new credit applications remained stable with a small uptick from 57.7 to 57.9, but dollar collections fell from 58.1 to 57.9. There was an improvement in the amount of credit extended, and it stayed above the 60 mark, moving from 62 to 63.

The numbers that caused the drop in the CMI were in the service sector's unfavorable factors. The unfavorable index is now teetering on the edge of contraction, slipping from 52.2 to 50.3. This matches the low point set in December 2011. All unfavorable indices fell, and only two remain above 50, whereas, in April, all were above 50. There were sharp drops in disputes, from 50.8 to 47.6, and dollar amount beyond terms, from 51.9 to 47.8. There was also a pretty sharp drop in the readings for bankruptcy filings, from 58.3 to 56.4, but was one of the two categories that stayed above 50 despite the fall.

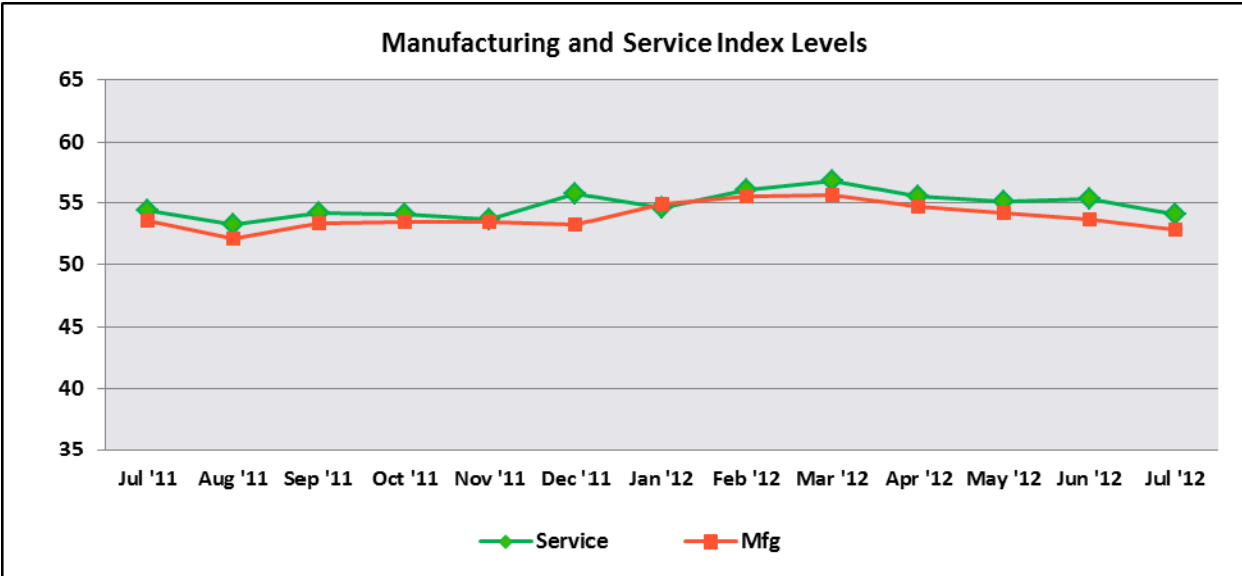
The service sector is a diverse collection of industries, and it is always a little tricky to identify the motivating factors from one month to the next, but this time the real damage seems to be in the retail sector. There have been some real declines in some store sales and the consumer keeps reporting that they are losing confidence. This fall has offset some of the better news coming from the housing sector. It looks as if the housing market finally found a bottom and is coming up for air. For the first time since 2009, the price of homes nationally started to trend back up, by a 0.2% rate. The reality is that many markets are still moribund, but there are some pockets of improvement that may become bigger factors later.

Service Sector (seasonally adjusted)	Jul '11	Aug '11	Sep '11	Oct '11	Nov '11	Dec '11	Jan '12	Feb '12	Mar '12	Apr '12	May '12	Jun '12	Jul '12
Sales	60.7	60.5	63.3	61.5	58.4	63.3	62.9	63.6	62.8	60.6	60.9	62.1	59.8
New credit applications	58.2	56.3	58.0	57.2	59.4	61.1	59.6	59.6	62.8	59.9	58.8	57.7	57.9
Dollar collections	57.1	57.9	58.9	57.0	57.6	64.9	56.7	64.5	60.7	59.4	57.3	58.1	57.9
Amount of credit extended	62.7	61.9	63.5	63.2	62.1	65.7	60.4	63.0	64.6	64.9	61.5	62.0	63.0
Index of favorable factors	59.7	59.1	60.9	59.7	59.4	63.8	59.9	62.7	62.7	61.2	59.6	60.0	59.6
Rejections of credit applications	51.2	50.1	49.8	50.9	49.4	49.1	49.9	50.8	51.6	51.8	51.8	52.2	51.6
Accounts placed for collection	50.3	47.8	47.8	51.3	47.5	49.3	49.6	50.7	52.5	50.7	52.0	49.0	48.7
Disputes	50.0	48.9	50.4	50.2	47.2	49.0	50.1	49.9	51.6	51.3	50.6	50.8	47.6
Dollar amount beyond terms	47.5	45.9	46.9	45.4	48.8	49.3	48.5	50.3	51.2	50.6	49.0	51.9	47.8
Dollar amount of customer deductions	49.9	49.3	50.2	49.8	48.9	48.9	51.0	50.6	51.5	50.4	51.0	50.9	49.7
Filings for bankruptcies	55.8	54.6	53.1	54.0	57.0	56.2	57.2	57.6	58.4	55.9	58.4	58.3	56.4
Index of unfavorable factors	50.8	49.4	49.7	50.3	49.8	50.3	51.0	51.6	52.8	51.8	52.1	52.2	50.3
NACM Service CMI	54.3	53.3	54.2	54.0	53.6	55.7	54.6	56.0	56.8	55.6	55.1	55.3	54.0



July 2012 vs. July 2011

The year-to-year trend is not very comforting at this stage. From February and March there has been a steady decline—not the trend that was shaping up at the start of the year.



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.*



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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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