BUSINESS INTELLIGENCE BRIEF

May 31, 2019

NATIONAL AND INTERNATIONAL NEWS AFFECTING LOCAL BUSINESS

Short Items of Interest – US Economy

- **More Tariff Threats –** The imposition of tariffs has become the go-to strategy for the Trump administration - regardless of the issue. Distress over the trade deficit with China results in a set of stiff tariffs, irritation with European policy begets tariff threats and now the ongoing concern over immigration has Trump threatening tariffs on goods from Mexico. Thus far these moves have yielded little other than economic disruption and increased stress on the US consumer. Tariffs are taxes and they are paid by the people who buy the goods that have been affected by the tariff and that means the US consumer. The nervousness within the investment community of late has been propelled by the threats of constant trade wars involving the US. The impact of all these additional taxes are starting to be a factor for consumers and business in general.

- **Q1 was Good but Not as Good as Thought –** The first revision to first quarter GDP numbers indicates that growth in Q1 was not quite as robust as was first thought but the decline was slight. It was at 3.2% and now is at 3.1%. That is still quite robust for what is often the weakest quarter in a given year. If there is any concern at this point it is that data showed less business investment, lower corporate profits and reduced consumer spending than was originally assumed. Not that the dip was all that significant but it has created some worry about what second quarter will ultimately look like as all this slowdown was towards the end of Q1.

- **Global Growth and the Fed –** Somehow many fail to notice how engaged the US is in the global economy. As has been repeated in these pages many times the export sector of the US economy is 15% of the nation's total GDP (over $2.7 trillion). What happens with the global economy matters and things are not looking good internationally. US tariff policy has triggered many trade wars and that has not helped matters. This has the Fed worried about the pace of the economy later in the year and that may influence their thinking on rate cuts. The Federal funds rate is still very low and hawks within the Fed would still like to see it go up but if global economic angst continues the Fed may consider a rate cut.

Short Items of Interest – Global Economy

- **Flight to Safety Accelerates –** Bond yields are crashing all over the world as investors begin to worry that Trump is determined to start a trade war with every nation on the planet. In the course of a week he has threatened China, Japan, UK, Germany, France, EU in general, Mexico, Canada and Turkey. The German ten-year bond is at an all-time low and the US ten-year is not far from its own record. The investment community is getting very nervous and this kind of attitude can be a self-fulfilling prophecy.

- **North Korean Executions –** North Korea's tyrannical leader has executed several high-ranking officials who had been engaged in talks with the US. They were deemed to have failed to get an agreement with Trump and therefore were put to death. Confirmed reports indicate that the five negotiators (including special envoy Kim Hyok Chol) were detained at the Mirim airport and were shot in the head. It remains baffling that any reasonable person in the world would wish to trust North Korea's psychopath in chief.

- **Latin American Economic Woes –** This year is not shaping up well for the nations in Latin America. The two largest economies (Mexico and Brazil) both experienced decline in the first quarter and there is not much confidence regarding a comeback given the fact that commodity prices have been down at the same time that both nations are dealing with low rates of productivity. Mexico is also getting hammered by trade hostility between them and the US. The latest slam has been the threats of higher tariffs. Brazil had hoped that closer ties would develop between Trump and Bolsonaro but that has yet to transpire.

Could This be a Trend?

Probably not but for the second month in a row the Credit Managers' Index showed improved readings. What follows is the executive summary of the CMI for May. If you want to see the entire report – complete with all the nifty charts and tables you can find it at the NACM website – www.nacm.org. Look for the Credit Managers' Index.

It might be useful to remind those who follow the Credit Managers' Index just why this is such an important tool for assessing the state of the economy. Why do people pay so much attention to the CMI and the index that inspired it – the Purchasing Managers' Index. It really comes down to four factors - timeliness, accuracy, lack of bias and predictive ability. They both track changes in the economy on a monthly basis, they both reflect consistent contributions from contributors, they both remain free of the bias that often occurs when someone is trying to manipulate outcomes and they both do a good job of predicting what is to come. The CMI is even better at this than the PMI given the reality of a credit manager's life – they are always more concerned about what is to come than what is happening right now. They want to know what shape a company will be in when it is time to pay the debt owed – 30, 60, 90 days (or more) ahead.

Having said all that, this month's CMI is trending in a positive direction for the second month in a row and that has not happened since August and September of last year. This month's reading for the combined score was 55.7 and it was 54.0 last month. The last time this reading was this high was in November of last year when it hit 55.8. The index of favorable factors rose pretty dramatically from 60.1 in April to 63.8 in May. Again, the last time numbers were this good was November of 2018. There was not a dramatic improvement as far as the unfavorable factors were concerned but it was an improvement as it moved from 50.0 to 50.2.

There was even better news in the breakdown for each sector. The sales category jumped from 61.0 to 65.9, a reading that was as good as those seen last year when numbers averaged in the high 60s (May at 69.6, June at 69.6, July at 63.9, August at 65, September at 68.8). The reading for new credit applications shifted up as well as it moved from 59.7 to 64.2 (highest point in a year). The data on dollar collections moved from 59.1 to 59.8 – not a big improvement but very solidly in the expansion zone. The amount of credit extended also saw a tidy gain as it moved from 60.6 to 65.4 – as high as that nice set of readings in November of last year.

There was generally good news as far as the non-favorables were concerned but the changes were not quite as dramatic. The rejections of credit applications fell a little but remained in the expansion zone. It was at 52.0 and slipped slightly to 51.8. The accounts placed for collection also fell a bit – from 48.5 to 47.0 and this has become a bit of a concern. This is essentially the last stage as far as credit is concerned and signals that something more drastic may be coming – such as bankruptcy. The disputes category stayed almost the same as it had been the previous month as it went from 48.5 to 48.6. The big improvement was in dollar amount beyond terms. It had been at 47.6 and this month it tracked at 51.3. In contrast to the news on accounts placed for collection this reading suggests that some companies are catching up with their credit obligations. The dollar amount of customer deductions remained very close to last month's readings with a score of 49.3 as compared to 49.7 the month prior. The filings for bankruptcies reading remained close to what it had been the month before – moving only slightly from 53.9 to 53.3.

The Purchasing Managers' Index this month fell pretty dramatically (and the New Orders Index fell even further) but both remained solidly in the expansion zone above 50. The readings from the CMI suggest that there may be less gloom ahead than might be indicated by the PMI as the favorable numbers all tracked strongly positive. The two indices seem to agree on current conditions and indicate that many companies are struggling with some of the economic headwinds related to trade concerns and a slower spending consumer.

Manufacturing Sector - Last month the manufacturing sector slipped a little while the service sector experienced some growth. The primary reason there was a hitch in the manufacturing sector is thought to be the issues of a trade war and the potential impact on US exports and imports. There has also been some concern regarding a slip in consumer confidence given that there continues to be confidence in the job market. The numbers from the latest Purchasing Managers' Index have been far weaker than was the case just a few months ago but they are still in the expansion zone. The changes in the CMI have been far more subtle.

The combined score for the manufacturing sector was 55.4 this month as compared to 53.7 last month and this is the highest reading notched since November of last year when it hit 55.6. The index of favorable factors rose sharply and jumped back into the 60s with a reading of 63.1 compared to 58.9 last month. The last time this reading was that high was in November of last year. The index of unfavorable factors rose very, very slightly from 50.2 to 50.3 but the important note is that this reading is still in expansion territory, if by the narrowest of margins.

The data from the favorable category was quite positive this month with all of the readings in the 60s. The sales mark reached 63.3 after sitting at 58.6 the month prior. This is the highest level reached since November of last year when it hit 64.2. The new credit applications also moved back into the 60 with a reading of 63.9 as compared to 59.8 in April. The dollar collections data also improved from 58.6 to 60.5 and there was a similar move from the amount of credit extended as it went from 58.5 to a whopping 64.6. The last time this reading was this high was (surprise!) in November of last year. Last month all the readings were in the 50s and this month all are back in the 60s.

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CMI Report (continued)

The data from the non-favorable categories is not quite as good but there is nothing catastrophic. The rejections of credit applications shifted down slightly from 53.1 to 52.5 but remained in the expansion zone. The accounts placed for collection also slipped but only by a small amount as it went from 49.3 to 49.0. The category still sits in contraction territory where it has been since February. The disputes numbers improved but stayed in contraction territory as it moved from 47.7 to 48.2. The dollar amount beyond terms category broke away from the contraction zone with a reading of 51.8 as compared to 48.5 the month before. It is a good sign that slow pays have not been quite the issue they had been. The dollar amount of customer deductions slipped deeper into contraction territory with a reading of 48.4 as compared to last month at 49.5. This category has not been out of the contraction zone for almost three years at this point. Filings for bankruptcies skidded a bit but stayed in expansion territory as it moved from 53.3 to 52.0.

The manufacturing sector has seen some mixed activity of late as there have been government moves that have been a clear benefit to some sectors and a clear inhibition to others. The steel and aluminum tariffs have been good for producers of the metal but not great for users. The tariffs on China have been good for some of those that compete with Chinese firms but bad for those that source from China or those that sell to China and are encountering their retaliatory tariffs and restrictions.

Service Sector - Last month the service sector was on something of a roll and it seems that this has extended into this month as well. The sector is a broad one and it is always hard to identify just what sector is creating the growth but it has been clear that retail has been strengthening alongside the construction sector. There have been signs of a slowdown in home building though and that might figure into future months. Meanwhile the summer travel season is about ready to start and that traditionally boosts retail activity. The overall index for service went from 54.4 to 55.9 and that is the highest point since November of last year (that was a VERY good month). The index of favorable factors jumped from 61.3 to 64.6 and the index for non-favorable factors escaped the contraction zone by moving from 49.8 to 50.1.

The favorable categories generally improved as sales moved from 63.4 to 68.5. This was a striking improvement and may end up being a bit of an anomaly when future readings are factored in. On the other hand, there have been similar readings in past months as it hit 69.4 in September of last year and 70.1 in June. The new credit applications also shifted up pretty dramatically as it went from 59.6 to 64.6 – as high as it was last May when the reading was 65.1. The dollar collections data slipped a tiny bit and that is a small concern. It was at 59.6 and is now at 59.1. These are obviously very robust numbers still but this is an all-important marker for the status of credit. The amount of credit extended shifted up sharply as well as it went from 62.7 to 66.3. This marks a return to the range that was common from May through November of last year.

The non-favorable categories were similarly mixed. The rejections of credit applications improved and that is a good sign given that there were more applications. There are times when the number of applications increase but there are more rejections and that signals that many applicants are not qualified and are desperately seeking somebody who will offer them credit. The accounts placed for collection sunk deeper into contraction territory and this may be the most concerning of all the readings. It was at 47.7 and is now at 45.1. This category has been in contraction for the majority of the last year (June of 2018 was the only exception at 52.0). There are clearly many companies now struggling with their debt and credit status. The disputes numbers also slipped but only slightly as they went from 49.4 to 49.0. The dollar amount beyond terms reading improved quite a lot and actually escaped the contraction zone with a reading of 50.9 as compared to 46.7. This was the first time this category had been in the 50s since the 54.3 notched in November of last year. The dollar amount of customer deductions also moved into expansion territory with a reading of 50.1 compared to 49.8 the month prior. The filings for bankruptcies stayed very close to last month's reading with a 54.5 compared to 54.6 in April.

Retail has been solid thus far this year but jumpy. The tariffs that have been indicated in the US-China fight have not focused on retail activity until this latest round and have only started to have an impact. The consumer is spending a little less on big ticket items like vehicles but more on "little luxuries" such as clothing and some sporting goods. There have been big retail gains for gas stations but department stores are not as robust as would have been expected.

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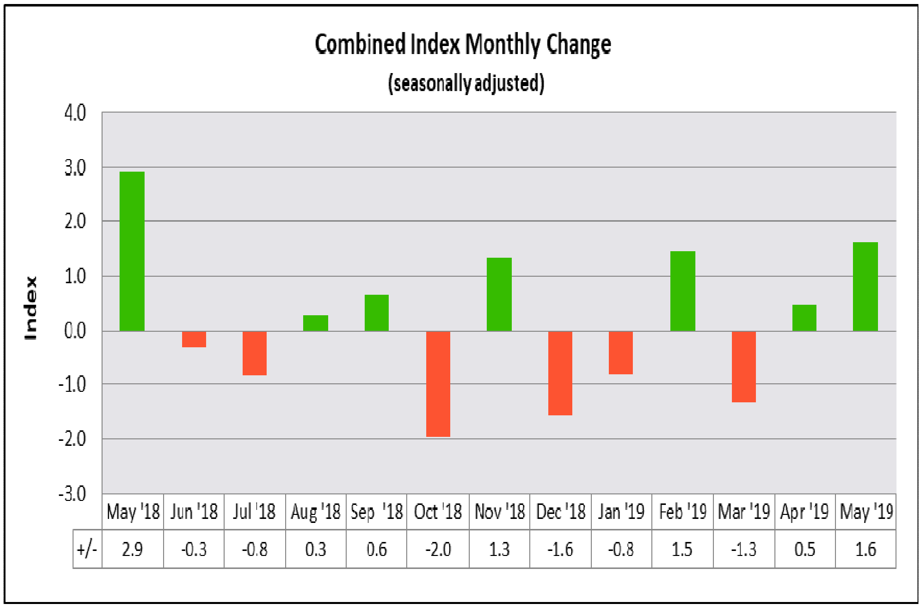

The chart above is the monthly tally of the Credit Managers' Index up and downs and it is good news that three of the last four months have been in positive territory and generally trending in a direction that promises more gains. There is still a wide disparity between the favorable and unfavorable sectors and that continues to signal that many companies are struggling to one degree or another. This is concerning as that kind of vulnerability can drag the index down in a hurry if there is a dip in the levels of sales or applications for credit – not to mention the all-important dollar collections.

Speaking this Month

06/05/19	Wichita	Kansas Society of CPAs	Public
06/06/19	Osage Beach	Missouri Society of CPAs	Public
06/13/19	Minneapolis	Minnesota Society of CPAs	Public
06/14/19	New York	NACM	Private
06/17/19	San Diego	Institute of Management Accountants	Public
06/19/19	Hilton Head	Chemical Coaters Association International	Private
06/20/19	Minneapolis	Minnesota Society of CPAs	Public
06/21/19	San Diego	North American Credit Services	Private
06/25/19	Kansas City	Mutual of Omaha Bank	Private
07/09/19	Kansas City	Plaza Club	Public
07/14/19	San Diego	IACC	Private
07/18/19	Iron Mountain	FHLB	Private
07/19/19	Lee's Summit	Lee's Summit Chamber of Commerce	Public

Decisions, Decisions

It is amazing how many of these we are called upon to make on a daily basis. Most are fairly minor – choices that do not really have life altering implications but it is somewhat intimidating to realize how many of these seemingly small decisions really will have a major impact on one's future. I have become much more aware of the decisions I make when it comes to the food I eat and have shifted a lot of behaviors. Gone are the sugary things and the sodas and the salt laden offerings. In their place come veggies and fruits and water. Then there are the attitude choices. As we get the garden in shape, we made the conscious choice to stop laboring in it and just sit back with a nice glass of wine and actually enjoy it!

Watching a show on wild weather brought home the importance of choice as well. Each segment featured people who made the wrong choice at the wrong time and nearly paid a fatal price. Steering the car into a brush fire when a turn the other direction would have been the correct decision. Electing to finish a run despite the arrival of a massive thunderstorm resulted in getting hit by lightning and losing a leg. In reality we can't always make the right call. Most of us do the best we can with the information at hand and more often than not that information is inadequate. I suppose the crucial thing is understanding one's priorities. If health is most important it is easier to choose to eat right and exercise. If the welfare of loved ones is a priority it is easier to avoid situations that might compromise that security. On the other hand, if the priority is impressing one's buddies it is likely that some pretty idiotic decisions will be made. This is why the most famous last words are "watch this" or "hold my beer".

What Do We Mean by Intelligence?

The name of this publication is the Business Intelligence Brief. Why did we call it that? All three words mean something to us and inform what we do. The first is business. This is a very broad term as there are tens of thousands of different businesses and they have only a few things in common. Our intent is to provide the kind of information that helps people understand the world and helps them grow their business and make bigger contributions to the companies they work for.

That brings us to the intelligence part. We believe in providing intelligence that is actionable and timely. The aim is to be able to anticipate what is to come so that contingency plans can be developed. We are not reporters; we will rarely be involved in "breaking news". We are analysts and we strive to provide answers to the key questions of "why" and "so what".

Finally – we strive to be brief. That is far harder than one would assume. The temptation is to go on and on in detail but that is too much to digest. We simplify when we can but encourage readers that want more to reach out and ask.

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