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The KG Index

Q3 2017

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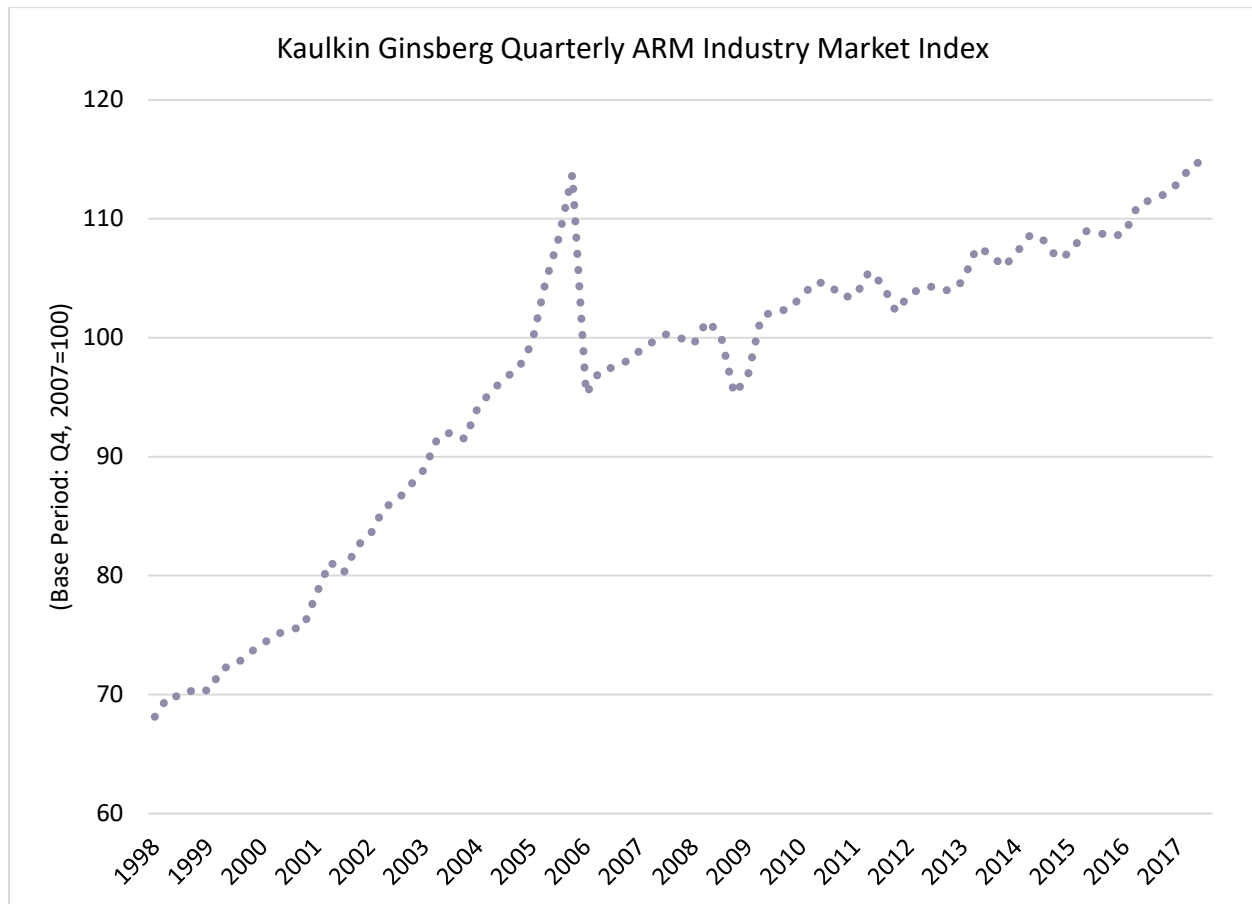
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The Economy's Effect on the ARM Industry: The KG Index



Q3 2017 data releases are complete, and that means it's now time to start analyzing the market conditions for the U.S. accounts receivable management (ARM) industry. Following a few upward revisions on performance data for Q2 2017, the index showed a slightly greater uptick than originally reported (114.57 vs 114.49), though the variance was nothing of significance. Instead, it just confirmed that Q2 2017 was a strong quarter for the ARM industry based on market conditions.

More importantly, Q3 2017 came in at an index value of 114.88. This indicates that the ARM index grew by 0.3% on a quarter-over-quarter basis with an annualized growth rate of 1.11%, which is down slightly from the 2.5% annual growth rate from Q4 2016. On the one hand, a lower growth rate for the index sounds like a bad thing since the market conditions aren't growing as rapidly. On the other hand, the market showed significant growth with little volatility since Q4 2015 so the slowdown is expected – especially since the ARM industry is a rather mature market.

Overall, the four key indicators contributing to our index – consumer bankruptcy filings, retail sales, official civilian unemployment rate (U3), and home price index – are trending positively. Here are a few of our notes on the current trends within each variable:

Consumer Bankruptcy Filings

In any given year, the first quarter is the second highest filing point while the second quarter is the greatest filing point during the year with the third and fourth quarters trending downward. However, the downward trend in filings for the third quarter of 2017 is more significant than previous years and may be indicative of economic growth and lower potential delinquent filings. Generally speaking, this does not provide ideal market conditions for the ARM industry since bankruptcy filings correlate with an increase in delinquent debt placements.

Retail Sales

While retail sales tend to maintain a long-term steady growth rate, the greatest period of growth is, unsurprisingly, concentrated in the fourth quarter of the year while other quarters are more flat. However, in 2017, the third quarter showed significant growth over the second quarter at approximately 2.6% vs a historical quarter-over-quarter growth average rate of roughly 0.6%. Considering reports of record setting retail sales for Black Friday and Cyber Monday, it looks like this trend will continue and contribute to positive market conditions for the ARM industry since the majority of these purchases run through credit cards and could spur an increase in financial services activity.

Official Unemployment Rate (U3)

The unemployment rate appears to defy most economic projections and is trending lower into territory not seen since the late 1990s and early 2000s. However, the quality of employment, as well as the labor force participation rate, dampens the significance of these measures slightly. As it relates to the ARM industry, a prolonged period of low unemployment rate tends to lead to negative market conditions unless it is offset by a relatively greater increase in consumer spending activity, which appears to be the case in 2017. Long-term, unemployment is expected to begin trending upward as more individuals rejoin the labor force, which aligns with the positive cyclical conditions of unemployment for the ARM industry.

Home Price Index

The home price index is positively correlated with revenue growth for the ARM industry and continues to trend upwards, which facilitates consumer confidence – especially in their ability to leverage debt – since homes account for the majority of most individual's wealth. Given current housing trends, it appears highly likely that the value will continue to rise over the next few years.

What to Look for in Q4 2017 Results

As 2017 comes to a close, monitoring the success of the retail sales and conversion of seasonal employees to long-term hires will be incredibly important since they drive consumption and the use of leverage by consumers and businesses alike. However, the “elephant in the room” is the potential effects from tax reform from the GOP since so much remains unknown, but it could lead to an increase in consumer confidence and business spending that would be good for the ARM industry's market conditions.

Please contact us at hq@kaulkin.com if you have any questions.