Kaulkin Ginsberg

The KG Index

Q4 2017

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About Kaulkin Ginsberg Company

Since 1991, Kaulkin Ginsberg has provided critical strategic advice to the outsourced business services industry. Our client-centric approach covers almost every stage of a company's life cycle and enables us to maintain longstanding relationships as trusted advisors.

Our Services

- **Mergers & Acquisition Advisory** – Develop an effective growth or exit strategy for your company. Our dedicated team will confidentially address your firm's financial performance and current market conditions, expertly guiding you through your M&A process.

- **Strategic Consulting** – Find solutions to challenges facing your business. Our experienced staff and external advisory network will work with you to create your long-term growth and eventual exit strategy.

- **Valuation & Financial Solutions** – Determine the fair market value of your business. Our sister company Topline Valuation Group provides technical, financial, operational, and benchmarking services to help you develop effective business strategies.

- **Market Intelligence & Analysis** – Shape and support your business decisions. Through our proprietary information service KG Prime, we arm you with the most relevant and timely data, enabling you to make informed decisions about the direction of your business.

- **Litigation Support & Expert Witness** – Build your case using the appropriate experts. Our findings have never been invalidated in any court or formal proceedings.

To confidentially discuss your interests, please contact us at hq@kaulkin.com or (301) 907-0840. For more information about Kaulkin Ginsberg, please visit www.kaulkin.com.

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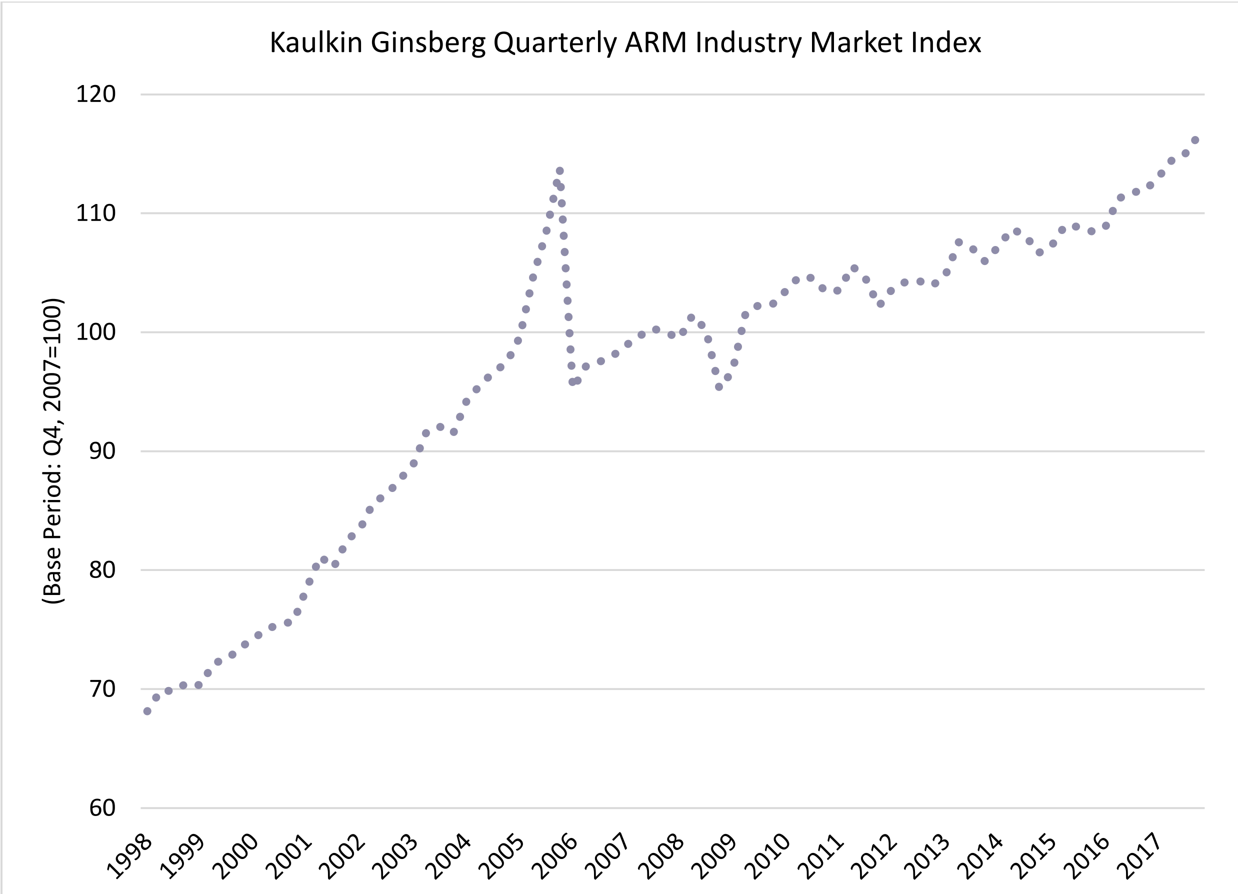
The Economy's Effect on the ARM Industry: The KG Index



Q4 2017 data releases are complete, and that means it's now time to start analyzing end of the year market conditions for the U.S. accounts receivable management (ARM) industry and discussing what you should look for in Q1 2018. Following a few revisions on 2017 performance data to prior quarters, we saw a slight drop in Q2 and increase in Q3. Overall, the ARM industry is trending upward based on these market conditions, which means that most agencies likely saw the positive effect on revenue during the second half of 2017 and first couple of months in 2018.

More importantly, Q4 2017 came in at an index value of 116.52. This indicates that the ARM index grew by 1.4% on a quarter-over-quarter basis with an annualized growth rate of 5.6%, which is up significantly from the Q4 2016 annual growth rate. On the one hand, a higher growth rate for the index sounds like a good thing since the market conditions suggest more rapid growth. On the other hand, the market's slow and steady growth tends to be less volatile, which may indicate a correction during the second half of 2018 since mature markets like the ARM industry typically grow at more steady rates. Additionally, these changes could be influenced by business and consumer reactions to the new tax law so it will be important to monitor this trend over the next few quarters.

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 and second quarters tend to be the highest points, while the third and fourth quarters trend downward through the year. However, this trend did not hold constant for the first time since 2008 with fourth quarter filings actually exceeding third quarter filings. While this may suggest an uptick in consumer filings in 2018, the total number of filings continued its decline from 2010 – the last year with positive growth in consumer bankruptcy 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 third and fourth quarters of the year, while the first and second quarters are more flat. However, in 2017 third quarter growth significantly outpaced the quarterly and annual growth rate of the fourth quarter. This suggests a positive market for the ARM industry since the majority of consumers tend to leverage these purchases through revolving credit lines and increases the potential for delinquent account filings.

Official Unemployment Rate (U3)

The unemployment rate appears to defy most economic projections and is hovering around 4.1% - a level 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 was the case in 2017. Confounding matters was the passage of GOP led tax reform, which may prolong low levels of unemployment for a while longer. However, it's yet to be seen whether or not tax reform will push wages meaningfully higher in 2018 and beyond. Overall, unemployment trends suggest positive market conditions for the ARM industry in 2018 with long-term unemployment expected to trend upward as more individuals rejoin the labor force.

Home Price Index

The home price index is positively correlated with 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 – especially since GOP tax reform allowed for homeowners to continue deducting some portion of the interest on their homes.

What to Look for in 2018

2017 ended on a high note for the ARM industry with strong market conditions that should carry over into 2018. Unemployment relative to wages and labor force participation should be monitored since these are indications of the success (or failure) of GOP tax reform. If it spurs increased economic growth, then consumers will likely increase their financial leverage with the corresponding increase in consumer confidence. However, if the economy stalls and the federal government lacks resources to facilitate fiscal policies due to a lower tax base, then the ARM industry may see the beginnings of a decline in market conditions that will provide some short-term gains for those that capitalize without overextending themselves. Contact us at hq@kaulkin.com if you have any questions.