PAYNET®

2017 Q3

Small Business Credit Outlook

Singing From a Different Hymn Book

The economy recently seems to be singing a tune in harmony with 3% growth. An economy in harmony means the various parts are expanding in sync with each other. Unfortunately, the private companies don't seem be in the same pitch as other parts.

Clearly, the high technology companies are singing loud and clear notes – they are creating great returns for their shareholders. Large industrials, while not the leaders in this stock market, are in tune with the high techs as far as growth, cash flow, and capital returns. Private businesses, however, seem to be carrying a different, less upbeat tune.

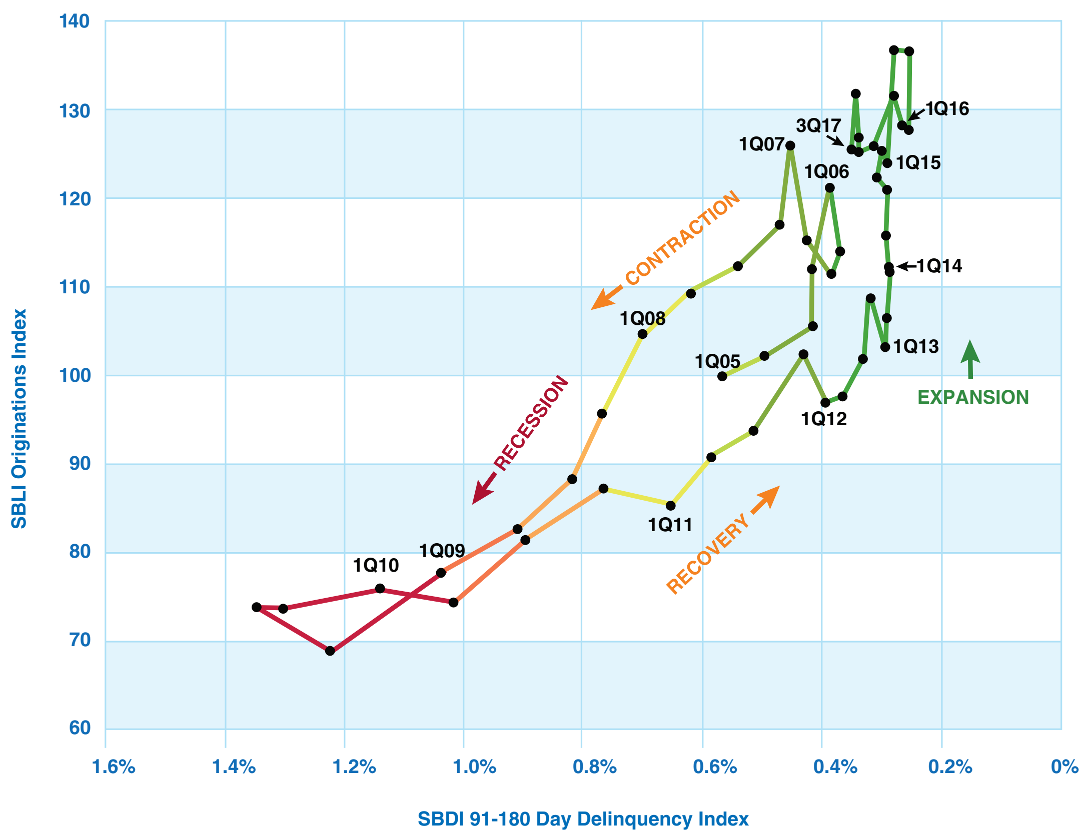
Business Cycle

The business cycle for private companies stalled during the last presidential election and has basically been unchanged ever since. Investment has remained about the same level since Q1 2016.

At that time, the PayNet Small Business Lending Index stood at about 128, whereas today, it is registering at 125 which shows private company investment has stagnated for nearly the past two years. Contrast this with tech stocks such as Amazon which has increased market value by 47% over the same period and as the S&P 500 which is up 18%.

Accompanying sluggish investment is slightly higher loans that are past due. From 1Q2016 to 3Q2017, loans severely past due have risen from 0.26% to 0.35%. While the business cycle for private companies remains in the low-risk expansion zone, clearly, they are just hanging in there.

PayNet Small Business Cycle®



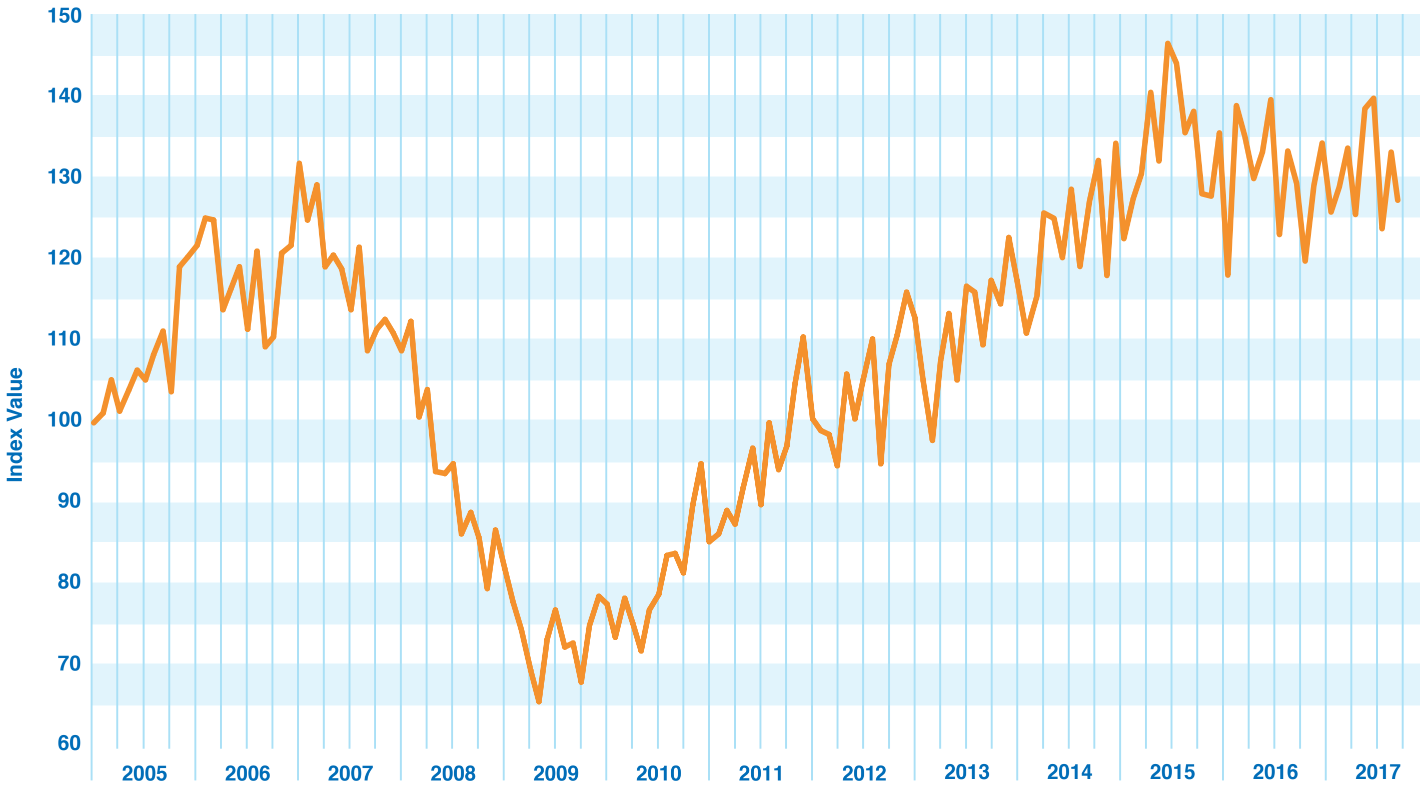
Recent Investment Activity

The Thomson Reuters/PayNet Small Business Lending Index fell 2% last month. This is a continuation of the theme of small business on hold.

Six of the nine months of 2017 have shown small businesses either making no change in their investments or shrinking them. Four of those months have shown outright contraction.

Thomson Reuters/PayNet Small Business Lending Index (SBLI)

(January 2005 - September 2017)



Credit Risk

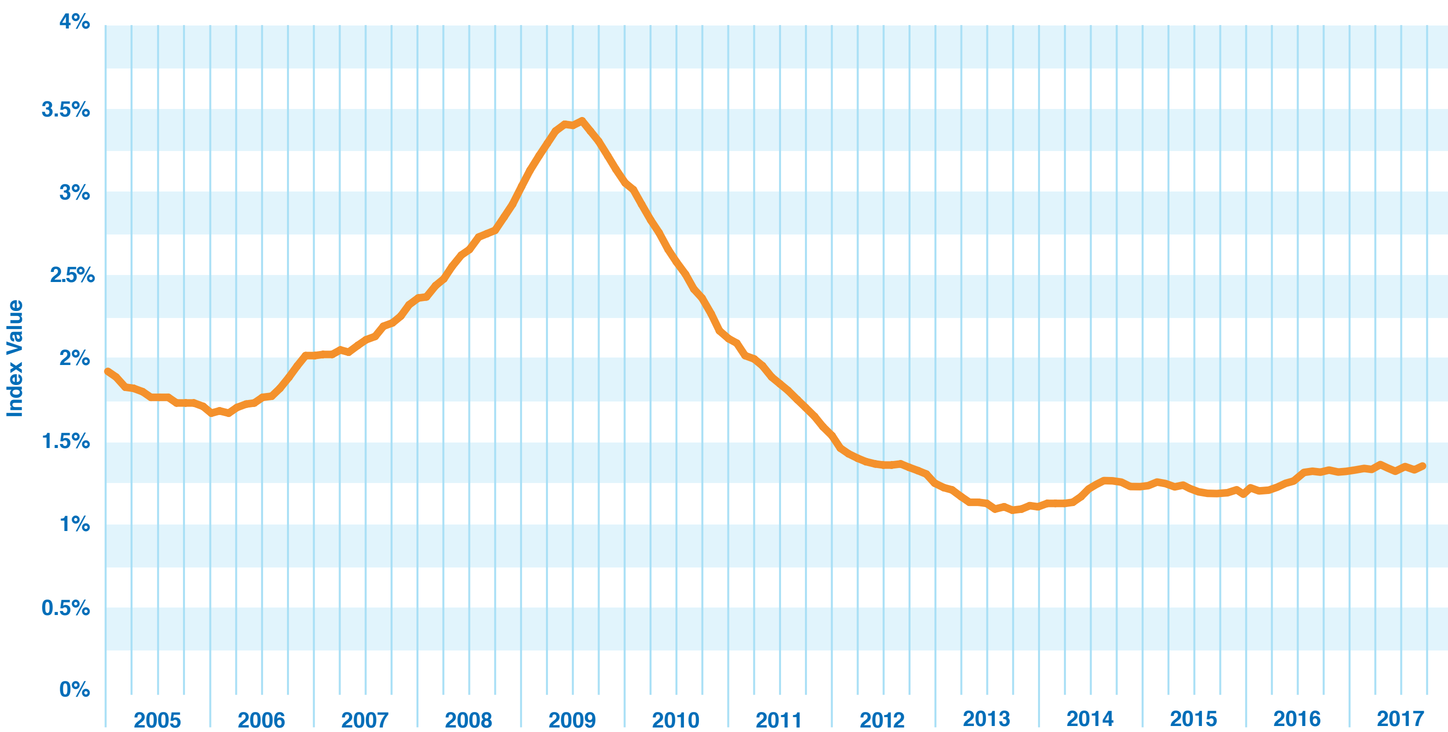
Financial health remains strong with the Thomson Reuters/PayNet Small Business Delinquency Index (SBDI) at 1.35% for loans 31-90 days past due in September 2017. This is an increase from 1.33% in August 2017, but still well below historic high levels.

As compared to one year ago, delinquency increased almost 3 bps (2%). Every month in the past year and a half has shown an increase; however, the year-over-year increase has been declining for the last five months, whereas this month it has increased slightly.

Transportation and Agriculture delinquency decreased 7 bps and 2 bps, respectively from August to September. The remaining segments showed delinquency increases of 1 to 2 bps.

The Thomson Reuters/PayNet SBDI for loans 91-180 days past due remained flat at 0.35% from August 2017 to September 2017. The Index is up 3 bps (8%) from one year ago. Healthcare, Retail, and Agriculture delinquency increased 3 bps, 2 bps, and 1 bp respectively from August to September. Transportation and Construction delinquency was flat, and the General segment delinquency decreased 1 bp.

Thomson Reuters/PayNet Small Business Delinquency Index (SBDI)
(31 - 90 Days Past Due)
(January 2005 - September 2017)



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Industry Analysis

While the pace of investment remains sluggish, a look at sectors underscores the fragility of this expansion at this time. Only four major sectors display positive year-over-year increases with Accommodation & Food, Administration, Construction, and Wholesale up materially. Eight major sectors are in contraction: Finance, Health Care, Manufacturing, Professional Services, Real Estate Leasing, Retail, Information Services, and Transportation.

In a sign of good news, Health Care, Retail, and Transportation are showing some increased investment over the past quarter which bodes well for these sectors. Only Accommodation & Food shows a negative trend for the quarter as a sign that the major sectors are not in a full-blown contraction mode. Overall, negative year-over-year performance combined with a more positive three-month trend means small business is in a wait & see mode.

Regional Analysis

While 5 of the 10 largest states show year-over-year declines, the trends indicate that the current doldrums could be replaced by higher growth over the next few months. If this trend continues, then, the largest states could very well add to GDP growth over the next quarter, reversing tepid performance since the presidential election.

Currently, North Carolina, Ohio, Texas, Michigan, and Illinois show signs of 1% to 7% growth over the prior year. California, Florida, Georgia, and New York are moving in the opposite direction with contractions from -3% to -0.3% now.

While growth and contraction are split almost evenly among the 10 largest states, 7 of the 10 are showing momentum towards expansion over the next few months. The recent 3-month average growth rate is positive for North Carolina, Ohio, Texas, Michigan, Illinois, Pennsylvania, California and New York. Only Florida and Georgia are showing a negative trend in their recent growth which means momentum in these states will likely remain negative over the next few months.

PayNet Small Business Lending Index

State	YoY % Change	3-Month Qtr. over Qtr. % Change
North Carolina	6.76%	2.92%
Ohio	5.58%	2.71%
Texas	2.03%	1.77%
Michigan	1.59%	1.37%
Illinois	0.39%	1.06%
Pennsylvania	-0.34%	0.13%
U.S.	-1.06%	0.60%
New York	-2.41%	0.04%
Georgia	-2.63%	-0.58%
Florida	-2.72%	-0.11%
California	-3.35%	0.68%

Credit Risk Outlook

The outlook for defaults for private businesses is on the rise as we can see from 9 months of actual defaults combined with our forecast for the remainder of 2017. This rise in defaults is partially due to slightly higher forecasted defaults in key large sectors of the private business economy like Accommodation & Food, Construction, Manufacturing, and Other Services (there are a lot of personal care, death care, dry cleaning, dental care companies on Main Street USA).

The sectors where defaults are falling offset this higher forecast for 2017 and 2018. Mining, Transportation, and Professional Services are showing lower defaults supported by lower loan delinquencies and improving economics. While some improvement will be seen from these smaller sectors, the large sectors of the private economy will likely show higher defaults in 2018 again as a result of factors such as slightly rising delinquencies and increased borrowing.

Historical and AbsolutePD® Forecast Default Rates

Industry Segment	Actual Historical Default Rates (1)		Forecast Default Rates (2)	
	2015	2016	2017*	2018
Mining	2.3%	4.9%	2.4%	2.1%
Transportation	2.6%	4.2%	4.2%	3.7%
Information	2.5%	2.2%	3.3%	3.1%
Professional Services	1.7%	2.1%	1.8%	1.8%
Agriculture	1.4%	2.1%	2.1%	1.7%
Construction	1.8%	2.1%	2.2%	2.5%
Accommodation and Food	1.6%	1.9%	2.3%	2.9%
Retail	1.8%	1.9%	1.8%	2.2%
Administrative Services	1.6%	1.8%	2.1%	2.3%
Manufacturing	1.5%	1.8%	2.0%	1.9%
Health Care	1.7%	1.8%	2.0%	2.1%
Other Services	1.2%	1.5%	1.6%	1.8%
Real Estate	1.0%	1.5%	1.5%	2.0%
Finance	1.2%	1.4%	1.5%	1.7%
Wholesale	1.3%	1.3%	1.5%	1.7%
Entertainment	0.9%	1.1%	1.1%	1.5%
Public Administration	0.6%	0.9%	0.8%	2.0%
Education	0.8%	0.9%	1.2%	1.8%
All Industries	**1.5%**	**1.8%**	**1.9%**	**2.1%**

Source:
(1) PayNet Small Business Default Index
(2) PayNet AbsolutePD®

$1.0mm or Less in Total Lease/Loan Exposure
*2017 Forecasts include 3 Quarters of actual defaults

Summary

While you'd like to have the choir all singing from the same hymn book; at times, some of the players get into other keys. Fortune 500 and big technology companies operate in different markets from private companies, which are usually captive to their local markets.

Private companies are not expanding their investments as are Fortune 500 and techs, likely because they face far different markets, financial profiles, and investing decisions than large companies. The good news is that private companies still have strong financial profiles and remain well positioned to add to GDP growth. They just need the right conditions.

About PayNet, Inc.

PayNet is the leading provider of credit ratings on small businesses enabling lenders to achieve optimal risk management, growth, and operational efficiencies. PayNet maintains the largest proprietary database of small business loans, leases, and lines of credit encompassing over 23 Million contracts worth more than $1.5 Trillion.

Using state-of-the-art analytics, PayNet converts raw data into real-time marketing intelligence and predictive information that subscribing lenders use to make informed small business financial decisions and improve their business strategy.

PayNet's small business capabilities range from historic credit-reporting and automated credit-scoring to detailed strategic business reviews that include portfolio risk measurement, default forecasting, peer benchmarking, and critical industry trend analysis.

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