Arizona Bank & Trust
a division of HTLF Bank

FINANCIAL FEED

2024.Q1

Fraud Trends and Best Practices

Tools and Resources to Help Fight Fraud

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FINANCIAL FEED 2024.Q1

As the Fed continues to wrestle with inflation and the labor war carries on, businesses across the U.S. displayed a great deal of resilience in 2023. Overcoming various post-Covid challenges, businesses are seeking informed guidance for 2024. As your reliable banking partner, we look forward to providing counsel and helping decision-makers manage their businesses with confidence. At HTLF, we've created the Financial Feed to provide our market with valuable insights on the future of finance. We hope these findings help you conquer potential challenges and capitalize on opportunities.

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Bill Callahan on the Arizona Market

Work with banking partners you can count on to help you achieve growth goals

It's still sunny economically in the greater Phoenix area and William (Bill) Callahan, President & CEO of Arizona Bank & Trust, a division of HTLF Bank, expects it to continue into 2024.

"It doesn't feel like business has dropped off dramatically," he said.

He's seen profit margins decline, but customers have created strategies to deal with changing economic realities.

Commercial and industrial customers make up about 75 percent of the bank's portfolio. Clients are building something, selling products or in service-related businesses. Their banking needs include financing, inventory and accounts receivable and access to general working capital.

MARKET ADVANTAGES

Arizona's economic health comes from creating diversity since the last recession. The Phoenix area has moved from its real-estate centric economy of 20 years ago to more technology, manufacturing and service-related industries.

"There was a conscious effort to diversify the economy away from real estate," said Callahan, a 40-year banking veteran.

Contributing to the effort is Taiwan Semiconductor, one of the world's largest chip manufacturers, who is building a plant in north Phoenix.

"That's a huge positive impact here. This time around it may be different if we ran into a recession. We're much more diverse. I think we've learned the lesson."

Bill Callahan
President & CEO

Also boosting the local economy is more people moving into Arizona than moving out — about 100,000 annually. Most of those are from 18-to-44-years old in their prime working and family-raising times, he said. Heading into winter the greater Phoenix area has a population of 5.5 million people.

"That's a huge positive impact here. This time around it may be different if we ran into a recession. We're much more diverse. I think we've learned the lesson," he said.

States like Arizona, Florida, Nevada and parts of California, where the housing market bubble burst in the Great Recession of 2007-09, were real estate dependent for many years. While real estate is still a large piece of the economic pie, it's less speculative than in the past, he said.

Education is a big niche. Callahan said his bank counts one of the country's largest charter schools, Great Hearts Academies, now in four states, as a client.

"We were an early pioneer in financing the charter school movement."

The bank has more than 10 charter school associations in their book of business, Callahan said.

Our bank also has a number of higher education clients, including Ottawa University. This growing university is based out of Kansas but has its largest campus in Phoenix.

Consumer debt has declined from almost 100 percent of disposable income to a smaller proportion. "So the consumer is not overburdened with debt today," Callahan said. "That's a positive for me."

Another advantage is housing values have not fallen, even though increasing interest rates have made upgrading or buying a new home challenging. Many have a mortgage interest rate of 3 percent versus a 7 or 7.5 percent rate if they refinanced or acquired a new mortgage.

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"Maybe it's something they haven't thought about or it reinforces something they're doing. You know anybody can rent money, but can you make a difference? You want to build these relationships with clients so you can help their business thrive."

- Bill Callahan, President & CEO

"So even though we're not seeing as many homes sell, there is no supply so that keeps values up. That's providing a wealth feeling for people whether they tap into it or not. It makes them more confident and that's an interesting dynamic."

Callahan is also optimistic about lower unemployment that stayed steady in 2023.

MARKET CHALLENGES

Inflation is a challenge in Phoenix as elsewhere.

"We're a couple years into pressures around higher inflation. You know, supply chain, people costs and all those kinds of things going on," he said.

"So no perceivable slow down, but everyone still has the people issue — finding adequate staff to do the things that companies need them to do," he said.

Passing along costs so far hasn't been a problem. But Callahan acknowledged the longer inflation continues, the harder it will be to manage.

"To me all the positive economic factors say the market feels like the Fed may be done raising rates into 2024. We might actually see the Fed have to take action to reduce rates and once that happens, I think the economy across the country is going to blossom."

WHAT YOU CAN DO

Understanding the business clients that the bank serves and how peers in the industry are succeeding has helped clients manage costs.

For example, a retailer client had capital invested in an eight-to-nine month product inventory which was hurting its cost structure.

The bank advised them about peer practices, with other similar stores keeping about half that amount of inventory on hand and reducing their expenses.

Companies go out of business because they run out of cash.

By understanding liquidity management in times like these, the company was able to reduce their inventory and maintain a healthier cash flow.

"Just tweaking numbers like that, you could see how much less they would have to borrow. And how much more they would have in their checking account," he said.

Our bankers are trained to listen to their clients and offer solutions by providing valuable information, making a difference in their bottom line. Offering research on top-performing peer-businesses across the country helps clients make better decisions.

"Maybe it's something they haven't thought about or it reinforces something they're doing. You know anybody can rent money, but can you make a difference? You want to build these relationships with clients so you can help their business thrive," he said.

HOW WE CAN HELP

Tools, like the bank's Commercial Card, are important to help manage cash flow, because it allows businesses to use the time from purchase to paying off the card to manage their money more strategically.

"The card picks up float for you. You have 30–45-day window before you have to make a cash outlay," he said. "We all know how to manage our cards. Whatever you put on it, you pay off every month. You don't carry a balance. It's a payment tool."

The bank also helps customers mitigate fraud with various products, especially Positive Pay.

Check fraud tops the list in the Phoenix area at about 75 percent of overall fraud, he said.

Positive Pay allows customers to review account numbers, check amounts and payee names before the bank pays the check. But Callahan says commercial cards are still safer if customers carefully monitor charges and report fraud within the required window of time.

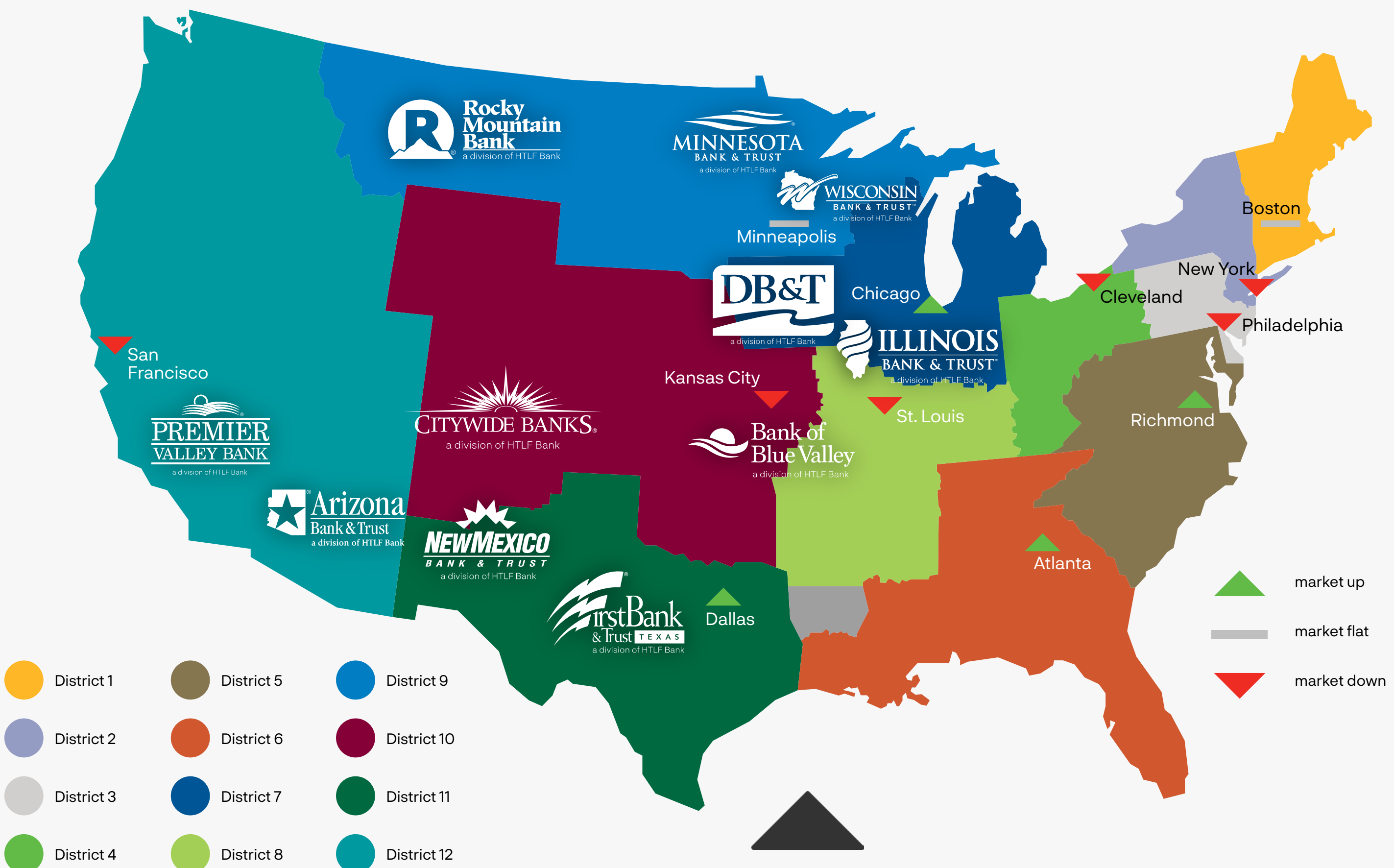
Larger companies use virtual or ghost cards that change account numbers with every transaction. "We build in a lot of safety measures to help our clients and we're here to support them."

National Economic Activity

From the Federal Reserve Bank's Beige Book

Commonly known as the Beige Book, this report is published eight times per year. Each Federal Reserve Bank gathers anecdotal information on current economic conditions in its District through reports from Bank and Branch directors and interviews with key business contacts, economists, market experts and other sources. The Beige Book summarizes this information by District and sector. An overall summary of the twelve district reports is prepared by a designated Federal Reserve Bank on a rotating basis.

ECONOMIC ACTIVITY WITHIN THE Federal Reserve Districts



On balance, economic activity slowed since October, with four Districts reporting modest growth, two indicating conditions were flat to slightly down, and six noting slight declines in activity.

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OVERALL ECONOMIC ACTIVITY

Retail sales, including autos, remained mixed; sales of discretionary items and durable goods, like furniture and appliances, declined, on average, as consumers showed more price sensitivity. Travel and tourism activity was generally healthy. Demand for transportation services was sluggish. Manufacturing activity was mixed, and manufacturers' outlooks weakened. Demand for business loans decreased slightly, particularly real estate loans. Consumer credit remained fairly healthy, but some banks noted a slight uptick in consumer delinquencies. Agriculture conditions were steady to slightly up as farmers reported higher selling prices; yields were mixed. Commercial real estate activity continued to slow; the office segment remained weak and multifamily activity softened. Several Districts noted a slight decrease in residential sales and higher inventories of available homes. The economic outlook for the next six to twelve months diminished over the reporting period.

LABOR MARKETS

Demand for labor continued to ease, as most Districts reported flat to modest increases in overall employment. The majority of Districts reported that more applicants were available, and several noted that retention improved as well. Reductions in headcounts through layoffs or attrition were reported, and some employers felt comfortable letting go low performers. However, several Districts continued to describe labor markets as tight with skilled workers in short supply. Wage growth remained modest to moderate in most Districts, as many described easing in wage pressures and several reported declines in starting wages. Some wage pressures did persist, however, and there were some reports of continued difficulty attracting and retaining high performers and workers with specialized skills.

The majority of Districts reported that more applicants were available, and several noted that retention improved as well.

PRICES

Price increases largely moderated across Districts, though prices remained elevated. Freight and shipping costs decreased for many, while the cost of various food products increased. Several noted that costs for construction inputs like steel and lumber had stabilized or even declined. Rising utilities and insurance costs were notable across Districts. Pricing power varied, with services providers finding it easier to pass through increases than manufacturers. Two Districts cited increased cost of debt as an impediment to business growth. Most Districts expect moderate price increases to continue into next year.

Most Districts expect moderate price increases to continue into next year.

Source: [The Federal Reserve's Beige Book](#)

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Outlook Across the 12th District

Previous softened economic activity leads to uncertainty

Twelfth District economic activity softened slightly during the October to mid-November reporting period. Labor market tightness eased moderately, and employment levels remained generally steady. Wages and prices rose at a slower pace relative to the previous reporting period. Retail sales were flat, and activity in the services sectors picked up slightly. Demand for manufactured products remained largely unchanged, while conditions in agriculture and resource-related sectors were mixed. Residential real estate activity softened, while activity in commercial real estate was varied. Conditions in the financial sector weakened further, and lending standards remained tight. Communities across the Twelfth District saw continued high demand for support services that was harder to meet due to declining charitable donations. Contacts expressed concern over a weaker economic outlook and increased overall uncertainty.

Arizona is part of the 12th District of the Federal Reserve Bank.

LABOR MARKETS

Labor market tightness continued to ease over the reporting period. Many employers reported improved availability and retention of workers in recent weeks as well as an uptick in job applications. Some employers, citing an uncertainty over the economic outlook, held staffing levels steady and only filled positions that opened up due to turnover. Employers in industries, such as legal services and aerospace, expanded their workforce in recent weeks, while some in manufacturing and financial services reported reductions in staffing. Nevertheless, employee turnover was reportedly elevated in hospitality and manufacturing. Several contacts expected the recent tentative agreement surrounding strike actions in the entertainment industry will bring back a significant number of workers in coming months.

Wage growth moderated across sectors as imbalances in labor market conditions for supply and demand continued to improve. Contacts reported budgeting annual pay raises in line with pre-pandemic rates. Recent layoffs in the financial services sector reportedly put downward pressure on wages within the sector. Wage pressures remained high for employers in legal services and some high-skilled trades across sectors. Some contacts highlighted upward wage pressures from the increases in minimum wages happening locally and ongoing labor union negotiations.

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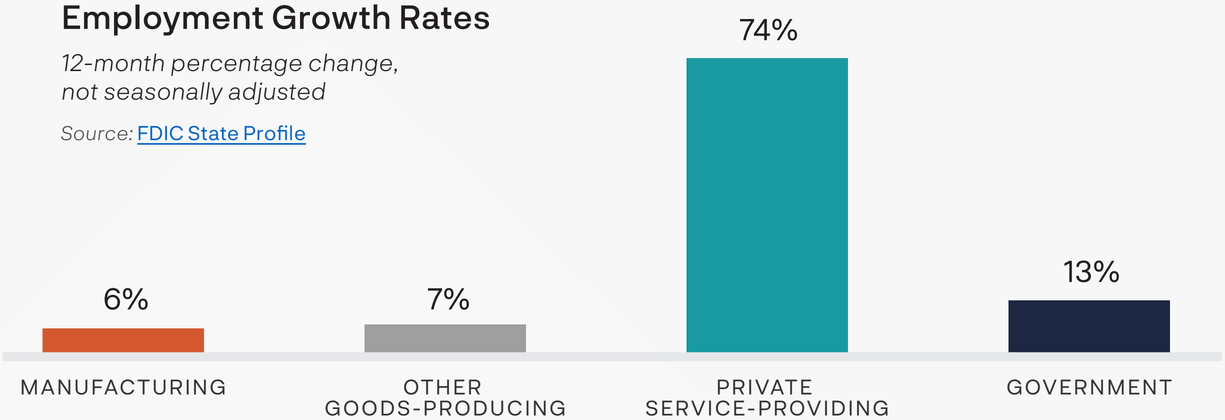
ARIZONA

Employment Growth Rates

12-month percentage change, not seasonally adjusted

Source: FDIC State Profile



PRICES

Prices remained elevated but rose at a slower pace relative to the previous reporting period. The recent drop in energy prices and signs of potential tapering overall demand growth helped alleviate some price pressures in recent weeks. Several contacts reportedly reduced fees for professional services in response to lower demand. Still, material and insurance costs continued to rise. In some instances, these costs were passed on to consumers, although one contact observed some pushback from customers to higher menu prices. Real estate firms noted that higher input, building and loan costs adversely impacted new construction projects.

RETAIL TRADE AND SERVICES

Retail sales were flat overall in recent weeks. Reports suggested some pullback in consumer spending on big-ticket items, such as motor vehicles. Demand was stronger for some product categories, such as groceries, fresh produce, and seafood. Retailers expected a solid holiday shopping season but noted that more discounts and offers than last year will be needed to entice consumers.

Activity in consumer and business services picked up slightly. Demand for leisure travel increased in recent weeks and was expected to rise further for the holiday season. Business demand for information technology, custodial, and security services increased, while demand for consulting services was down. Several contacts expected the end of strike actions in the entertainment industry to spur growth in the Southern California economy, although some feared that many local businesses and services providers would be unable to recover losses for an extended period.

MANUFACTURING

Manufacturing activity was unchanged at robust levels in recent weeks. Manufacturers reported continued general strength in the sector and solid demand for heavy machinery, capital equipment and fabricated metal products. The aerospace industry reportedly saw an uptick in orders in recent weeks. Food manufacturing and packaging continued to operate at or near capacity. Reports indicated continued improvements in raw materials availability and supply chains, although some manufacturers mentioned lingering delivery delays.

AGRICULTURE AND RESOURCE-RELATED INDUSTRIES

Conditions in the agriculture and resource-related sectors were mixed. Across the District, crop yields were generally at or above historical averages, particularly for apples. Domestic demand from the food services and retail sectors was solid but showed some signs of easing in recent weeks, and exports for some products such as nuts rose. Producers commanded lower prices for products such as fish and nuts and expected apple prices to fall due to the strong harvest. Costs for fuel, packaging, labor and equipment rose, while irrigation and international shipping costs declined. One contact in Utah cited notable reductions in the cost of feeding livestock as ample growth of grasses on grazing lands lowered demand and prices for hay.

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REAL ESTATE AND CONSTRUCTION

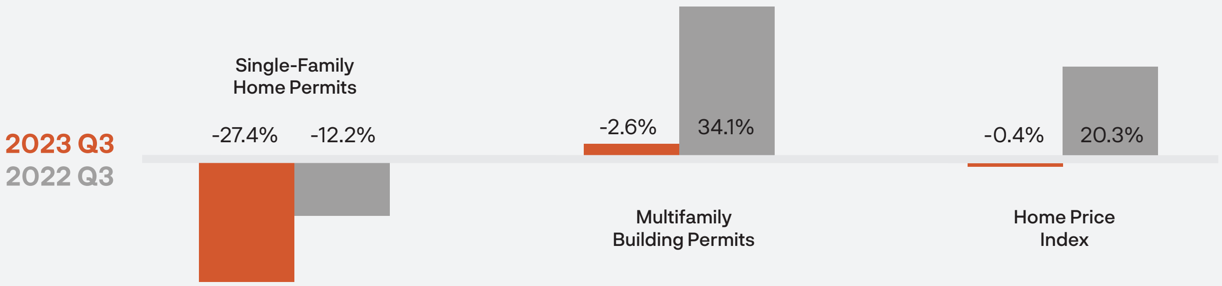
Conditions in the residential real estate sector softened further over the reporting period. Asking and selling prices for single-family homes declined as buyers were deterred by high mortgage rates, and demand from first-time w was particularly weak. Inventories remained low, and properties took longer to sell. Contacts reported slight softening in the multifamily sector with lower occupancy rates in some downtown high-rise buildings and slower rent growth. In contrast, a Southern California contact noted continued strong demand for affordable multifamily units. New residential construction was stable, while renovation construction rose as homeowners sought to modify existing homes rather than buy new ones.

New residential construction was stable, while renovation construction rose as homeowners sought to modify existing homes rather than buy new ones.

ARIZONA
Other Economic Indicators

(not seasonally adjusted)

Source: *FDIC State Profile*



Asking and selling prices for single-family homes declined as buyers were deterred by high mortgage rates, and demand from first-time homebuyers was particularly weak.

Commercial real estate activity was varied in recent weeks. Office leasing activity was muted, and occupancy rates remained low. In contrast, demand for space in sectors less conducive to remote work, such as defense and lab-based sciences, was robust and occupancy rates were high. Elevated financing costs and economic uncertainty slowed commercial construction projects. A contact in Utah reported that construction continued as planned on existing industrial projects, but that rent growth in this sector began to ease.

Source: The Federal Reserve's Beige Book

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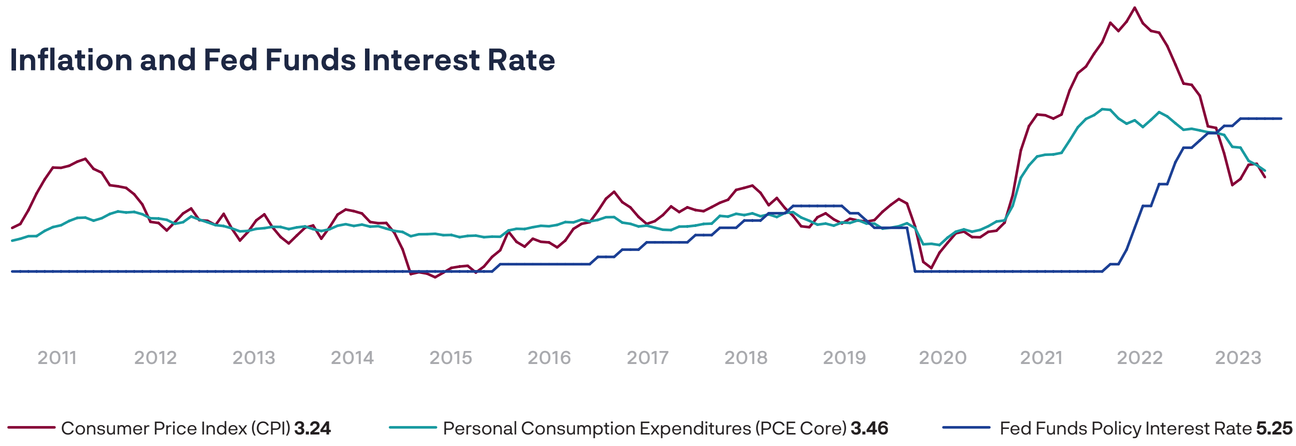
The Recession of 2024 Might Surprise Everyone

PAUL DICKSON, DIRECTOR OF RESEARCH, VP

A year ago, a headline "The Recession of 2023 might surprise everyone" would have been prescient simply because it didn't happen. On the contrary, last year showed surprising resilience and a pace of growth no one expected, despite forecasts of a slowdown or recession by most economists. 2023 was supposed to have been the year in which the economy succumbed to the sharpest increase in interest rates in four decades; tightening lending standards by the banks; and the end of pandemic-era government spending. Accumulated savings from Covid-related shutdowns and receipts of stimulus checks were expected to have run out well before the end of the year helping foment a recession. This did not happen in 2023, but chances seem higher for 2024.

Inflation and Fed Funds Interest Rate



THE FEDERAL RESERVE'S FINALE

At December's Federal Reserve Open Market Committee (FOMC) meeting the members indicated that the cycle of rate hikes has ended. Most of us opined that the policy interest rate (Fed Funds) will be cut several times through the course of the year. It appears (see Inflation and Funds Interest Rate graph) that inflation is on a path to the Fed's 2% target, fulfilling the first part of its "stable prices and full employment" mandate. The challenges to achieving that goal are the tight labor market, persistent and surprising housing inflation, and economic activity being bolstered by an unanticipated boom in investment.

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LOOKING FOR SLACK IN THE LABOR MARKET

The unemployment rate hit a 50-year low at the end of 2022. At the same time, the number of job openings skyrocketed to double that of the unemployed. This data and mounting labor action sparked worries of a wage-price spiral akin to those of the 1970s. Job openings have declined but remain historically high compared to the number of jobless and the unemployment rate remains near all-time lows and at levels once deemed unlikely. Having succeeded in the second part of its dual mandate — full employment — the Fed wants more slack to feel comfortable.

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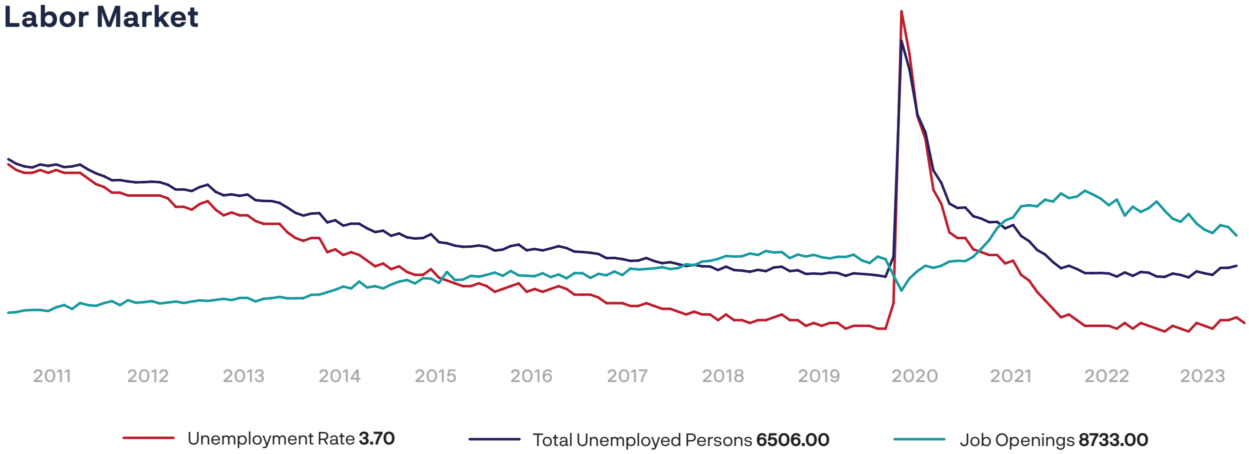
Labor Market



Paul Dickson, Director of Research, VP, joined HTLF in 2012 and brings over 20 years of industry experience with him. His specific area of expertise is fixed income investing and he assists with global economic and risk analysis. Paul was previously the head of JP Morgan Asset Management's Emerging Markets Fixed Income team managing $6 billion in assets. Prior to that, he was a senior bond strategist at Lehman Brothers and was a founding member of Chase Manhattan Bank's first Emerging Markets Research Group. He holds dual master's degrees in Economics and International Studies from Johns Hopkins School of International Studies in Washington, D.C.

Paul Dickson
Director of Research, VP

HOUSING DILEMMA

Inflation measures have been skewed higher due to the tight housing market. Representing more than a third of the inflation indices, housing or shelter prices play a dominant role. Measured by surveys rather than transactions, the slowdown in home sale volume and the decline in actual sales pricing is not captured. Instead, the persistent housing shortage, estimated to be near 4 million units, has led to an overestimation of value by people surveyed. The Federal Reserve had hoped that a rise in mortgage rates would set off a decline in home prices due to a lack of affordability. Paradoxically, the rise in mortgage rates has led to a decline in home availability, because those who enjoy low mortgage rates are less likely to sell. This has supported higher prices, rather than lower ones. Recently, Fed officials have noted this issue publicly and a “Supercore” inflation index that excludes housing in addition to food and energy has become popular as it may show a better metric.

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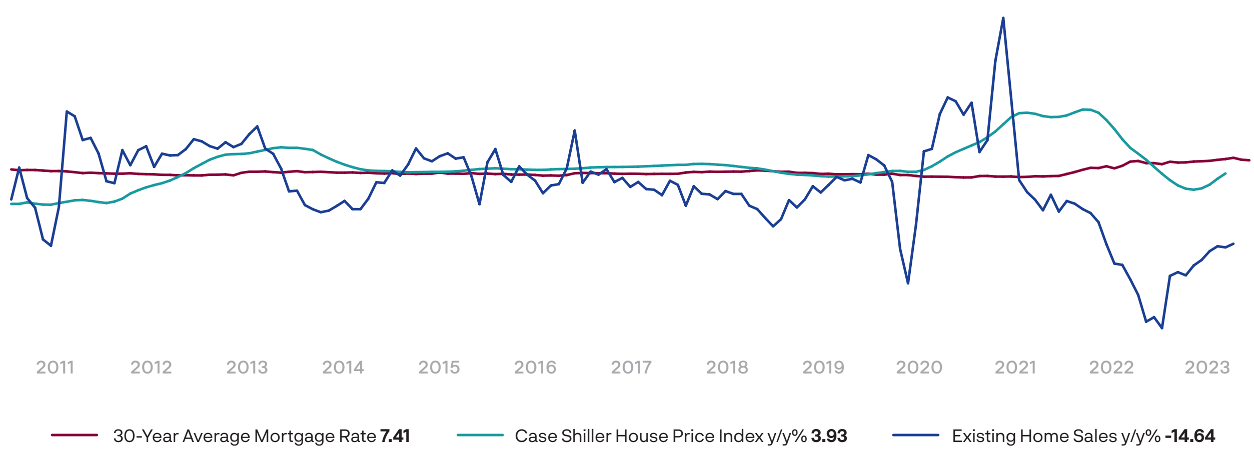
Housing Market



SPENDING AND INVESTMENT

Economic policies such as the Infrastructure Investment and Jobs Act, CHIPs and Science Act, and the Inflation Reduction Act have heightened spending and investment by the government directly and incentivized private industry to do so as well. These have contributed to an economy already buoyed by robust consumer spending and helped forestall the expected slowdown over the past year.

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THE OUTLOOK FOR 2024

Expectations from the start of 2023 are repeating themselves for 2024. The bond market is pricing a series of interest rate cuts starting in the Spring on the belief that inflation will continue to fall towards the Fed's target of 2% and implying that those cuts will be necessary as the economy flirts with recession. There have been studies suggesting that the Covid-era savings have been depleted among lower income households and soon will be for everyone else. Credit card balances have risen significantly. This coincides with a significant rise in payment delinquencies for credit cards, auto loans, and mortgages. The recent resumption in student loan payments adds another source of stress for millions of consumers. Higher mortgage rates have slowed home sales, and this will dampen activity in many related sectors from construction to household appliances. The commercial property sector has not recovered from Covid-era work transitions and is under pressure from higher interest rates, lower valuations, and more limited prospects. Private credit markets, undermined by higher interest rates, may be hiding vulnerabilities so far undetected. These developments imply a more fragile economy in the coming year and a growing likelihood of recession.

The bond market is pricing a series of interest rate cuts starting in the Spring on the belief that inflation will continue to fall towards the Fed's target of 2% and implying that those cuts will be necessary as the economy flirts with recession.

The Federal Reserve has significant room to cut interest rates to counteract a sharper than expected economic decline. Timed right, a soft landing could still take place even if the bad news outweighs the good.

Standing in opposition to a recessionary outcome is an economy starting from a reasonably strong position. Unemployment remains near a multi-decade low and a small rise, while unfortunate for those put out of work, would be more in line with historic norms. A softening of this tight labor market would be a relief for policymakers, and many firms still need to fill vacant positions. In aggregate, consumer balance sheets are in good shape with debt to disposable income being in line with historic norms. Rising credit card debt is far from being worrisome so consumers have significant borrowing capacity. Most of the banking sector is in good shape and the systemic problems that led to the Global Financial Crisis of 15 years ago are not apparent. House prices might come down in some markets, but with a housing shortage still generally present, a serious downward spiral is improbable. Finally, the Federal Reserve has significant room to cut interest rates to counteract a sharper than expected economic decline. Timed right, a soft landing could still take place even if the bad news outweighs the good.

On balance, a mild recession in the second half of the year seems likely. But the title of this article could also prove prescient when one fails to occur. ▲

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FRAUD

Trends and Best Practices

Fraud continues to be a challenge for many organizations. According to the 2023 Association for Financial Professionals, 65 percent of organizations report that they continue to be targets of fraud. And as the payments landscape continues to evolve, fraudsters are evolving their tactics too.

Targets of Payments Fraud

Check issuing continues to decline as the number of organizations using digital payments increases. The mass adoption of digital payments is partly due to the remote work environment. Electronic payment usage increases may also be the reason there has been an uptick in ACH fraud. However, checks continue to be the primary target for fraudsters.

63%
CHECKS

36%
CREDIT CARDS

31%
WIRE TRANSFERS

30%
ACH DEBITS

30%
ACH CREDITS

Integrated Payables

One payment solution for all payment types

Integrated Payables is truly the complete commercial payments solution for all payment types, and it benefits both you and your vendors. Build better relationships with them, and give valuable time back to your employees so they can better focus their efforts on the success of the business.

Scan here to get started
building better relationships with vendors, and give valuable time back to employees so they can better focus on the success of the business.

Leading Source of Fraud: Business Email Compromise

Fraudsters continue to exploit businesses via business email compromise (or "BEC") with 71% of organizations experiencing these fraud attempts or attacks. Although this is an increase from 68% in 2021, the study found that this year, fewer, smaller organizations were targets of BEC fraud. This may suggest that the implementation of controls and measures organizations have taken to mitigate fraud have been successful.

BEC is a scam targeting business' payment processes. Essentially, a fraudster takes over valid business email accounts through social engineering or computer intrusion techniques to process or initiate unauthorized transfers of funds. The individual responsible for processing payments is tricked into thinking the request is valid, coming from a company leader, partner or third-party vendor, and processes the payment.

Payment Methods Impacted by BEC

45%	34%	26%	16%	8%
WIRE TRANSFERS	ACH CREDITS	ACH DEBITS	CHECKS	CREDIT CARDS

BETTER PROTECT YOUR BUSINESS

Safeguarding your assets begins with awareness and recognizing that prevention is an ongoing critical business strategy. Fraudsters are always searching for new schemes to capture funds from their victims. When they plan their attacks, they are looking for vulnerabilities in an organization's payment controls and processes. There are several steps a business can take to mitigate fraud and avoid potential financial losses.

Best Practices to Fight Fraud

CONDUCT ONGOING EMPLOYEE TRAINING

Employees are the gatekeepers of your organization With proper training, they can more effectively safeguard your financials. AP/AR departments are often in the fraudster's crosshairs, so training and following strong policies in those departments are particularly crucial.

Possible training topics include:

- Defining fraud and the consequences
- Presenting examples of fraud the company may be exposed to
- Reviewing policies/ controls to prevent internal and external fraud
- Practicing recognizing fraud indicators and red flags
- Reviewing the steps to report suspected and actual fraud

REVIEW INTERNAL CONTROLS AND PROCEDURES

Strengthening internal controls and procedures is the greatest fraud deterrent.

Below are a few controls/ procedures to consider:

- Establish a limit per account and/or employee
- Separate responsibilities to establish checks and balances
- Require approval on all payments
- Set limits based on payment history
- Reconcile activity daily to identify suspicious payments, giving the company the opportunity to stop and/or recover fraudulent payments

IMPLEMENT VERIFICATION PROCESSES

Additional verification before submitting payment could make all the difference in identifying fraud and preventing financial loss. Implementation involves updating policies/controls and educating employees on the updated payment processes.

Consider the following:

- Changes in payment information must be verified by calling the phone number on file for the vendor
- Adding a new vendor requires approval from multiple employees
- All payments requested via phone or email must be verified by calling the phone number on file for the vendor
- Large payments should prompt for approval from management

TOOLS AND RESOURCES TO HELP FIGHT FRAUD

Strong policies, continuous employee education and accessible fraud tools and resources can help to mitigate fraud. AFP reported organizations use the following practices to help reduce fraud risk:

FIGHTING CHECK FRAUD

92%

USE CHECK POSITIVE PAY

79%

USE PAYEE POSITIVE PAY

FIGHTING ACH DEBIT FRAUD

51%

USE ACH POSITIVE PAY

79%

USE DAILY RECONCILIATION

Download Fraud Prevention Guide

Source: [Association for Financial Professionals: 2023 Payments Fraud and Control Survey Report]

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Contact Arizona Bank & Trust, a division of HTLF Bank today to speak with a commercial banker. Together, we can **build a fraud prevention strategy to help protect your business** in mitigating fraud risk.

Thriving vs. Surviving?

Wise Liquidity Management Moves for Businesses in All Seasons

The economic forecast may be uncertain, but preparing for inflated rates is the smartest course of action. Liquidity management is a lot of work, but the benefits can help your business thrive rather than survive. Learn more about how you can keep your business afloat in every season.

A fluctuating economic environment, such as the one we're currently experiencing, has historically pointed toward the imminent possibility of a recession. While forecasts aren't 100% reliable, proactive leaders should prepare for economic turmoil by reimagining their company's liquidity management.

Under these economic conditions, weathering the storm is a matter of preparation. Streamlining your cash flow can build resistance against outside economic forces.

It is possible to increase your working capital without bringing in additional revenue. You simply need to increase the efficiency of your cash conversion cycle (CCC). Regardless of whether inflation persists, you'll benefit immensely from addressing stagnations within your CCC. And should a recession occur, companies with increased access to working capital will hold a significant advantage.

There are several strategic liquidity management moves you can make to shore up your company's financial health.

The following key steps can help you remain agile in a challenging environment.

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1 IMPROVE VISIBILITY ON YOUR CURRENT FINANCIAL PERFORMANCE

Your financial data provides a comprehensive overview of your CCC and empowers you to identify and address otherwise unnoticed issues. Visible treasury data enables you to leverage your internal insights to adapt more quickly—a feature that can make or break businesses in a volatile economic environment.

However, finding the right liquidity management techniques for your CCC requires a detailed understanding of your position. So, to this end, let's review some of the key terms and factors that will determine which strategic course of action is most viable for your company.

LIQUIDITY MANAGEMENT AND MEASUREMENTS

First, a quick overview of the fundamentals. A company's liquidity is measured by the ratio of assets that can be converted to cash against debts due over the next year.

Volatile markets have significant impacts on this ratio. For example, liquidation might take extended periods due to factors like supply chain backups.

Liquidity management refers to the oversight of working capital to meet a company's financial obligations and, hopefully, optimize its yields.

NET BORROWERS VS. NET INVESTORS

Net borrowers are organizations that borrow more than they lend or save. Over time, excessive debt accumulation can lead to an unmanageable burden, especially in volatile economies with rising interest rates.

Some industries necessitate operating as net borrowers. In these cases, high liquidity management is needed to meet obligations. Optimizing your CCC is critical when operating within this business framework.

Net investors, on the other hand, generate enough capital to cover their costs, making them more resistant to volatile interest rates. However, net investors aren't immune to economic challenges. CCC optimization can still protect them from market changes. Plus, shortening the cycle can yield significant returns.

CASH CONVERSION CYCLE OVERVIEW

Your cash conversion cycle is a simple calculation of how long you can bear the costs of making or providing your goods or services before you receive payment. Shorter cycles add value to a company by increasing liquidity and enjoying fewer funding requirements.

Optimizing your CCC is the process of streamlining cash flows to increase the amount of working capital your company has access to at any moment. Three essential elements form the CCC:

- **Days Inventory Outstanding (DIO)**

  Days Inventory Outstanding (DIO) measures how long it takes to convert raw materials into products or services. Issues with DIO management can result in unnecessary inventory storage costs or supply chain delays.

  Reducing the time frame of your DIO contributes to a lower CCC, as capital spends less time tied up in physical products. However, many companies are rethinking the just-in-time approach after manufacturing bottlenecks disrupted their operations during the Covid-19 pandemic.

- **Days Sales Outstanding (DSO)**

  Days Sales Outstanding (DSO) tracks the average time you collect payments after a sale. Reducing your DSO is also advantageous because it accelerates receivables and increases the speed of your CCC.

  Digital solutions that automate accounts receivable (AR) department processes can drive down time frames by increasing customer convenience and speeding up transactions.

- **Days Payable Outstanding (DPO)**

  Days Payable Outstanding (DPO) describes the average amount of time it takes for your company to pay suppliers after delivery. Expanding your DPO time frames contributes to an efficient CCC by keeping working capital in your company's hands longer. Larger companies are often able to obtain extended payment terms from smaller suppliers.

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Establishing benchmarks to measure your financial performance is one of the best ways to streamline your capital management. No company can maintain viability if, in the long term, its cash inflows don't exceed its cash outflows.

2 ESTABLISH WORKING CAPITAL BENCHMARKS FOR YOUR BUSINESS

Establishing benchmarks to measure your financial performance is one of the best ways to streamline your capital management. No company can maintain viability if, in the long term, its cash inflows don't exceed its cash outflows.

In other words, there must be enough incoming capital to meet obligations. This is known as a positive cash flow. It differs from profitability, yet it's an essential metric to track. Maintaining access to working capital to fund operations is critical.

Benchmarks generally compare your industry competitors' performance against your own. The goal is to find operational lags or issues with your cash flow that could impact your long-term financial health. Because the measurement is industry-specific, you'll need to determine which metrics are meaningful to optimize your operations fully.

For instance, businesses without inventory, such as software companies, will obviously not need to track their DIO. However, because liquidity management is critical across industries, slimming down your CCC can be done by examining several cash flow key performance indicators (KPIs).

Most notably, reducing your DSO and increasing your DPO significantly shortens your CCC. As a result, you can increase your positive cash flow. However, extending your DPO too far puts your future credit terms at risk. So, if your DPO benchmark falls behind the industry standard, you should renegotiate better terms.

Of course, the other half of the equation is to set your DSO against similar industry benchmarks. If you're experiencing delays relative to these industry standards, you should investigate faster ways to collect. Or, you could perhaps offer incentives to encourage early payments.

Your company will have unique benchmarks to track and compare. An experienced banking partner can help you set and manage your cash flow KPIs.

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3 OPTIMIZE WORKING CAPITAL MANAGEMENT THROUGH TECHNOLOGY

Across different industries, companies are quickly turning to digital solutions for liquidity management and CCC optimization. The Covid-19 pandemic only accelerated the digitization of treasury management systems, as efficient remote processes became operationally critical.

Today, many companies still use manual or paper processes in their accounts payable (AP) and AR departments. Although, companies clinging to these outdated systems likely won't be able to compete with those using artificial intelligence (AI)-driven automation to increase speed, accuracy and data visibility.

Modern treasury technology is beneficial in a volatile economic environment. The comprehensive information sets generated from sophisticated digital treasury systems can provide the necessary information to compare your results with relevant industry benchmarks.

In fact, through advanced technology, you can carefully navigate an inflationary cycle with meticulous liquidity management to potentially gain a competitive edge.

Modern treasury technology is beneficial in a volatile economic environment. The comprehensive information sets generated from sophisticated digital treasury systems can provide the necessary information to compare your results with relevant industry benchmarks.

LIQUIDITY MANAGEMENT ACROSS INDUSTRIES

Of course, while treasury technology advances are ideal across sectors, your industry will largely determine the best approach to optimize your working capital management.

For instance, retail companies' most common cash flow bottleneck is the gap between inventory purchases and sales. This can be extensive, especially when gearing up for the holiday season.

Treasury technology can help solve these issues by streamlining your accounting processes and freeing up your AP department's time to focus on supplier relationships. Negotiating better terms may also help retail businesses avoid borrowing from a bank to cover costs.

On the other hand, manufacturing companies that sell goods on credit commonly experience cash outflow issues. This is because significant costs are incurred during the manufacturing process.

In response, manufacturers can use their convenient treasury technology to request payment prior to production. This can greatly reduce manufacturing CCCs and increase access to working capital.

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4 UNLOCK “TRAPPED” CASH

The ultimate effect of modern treasury management technology is to free up stagnant cash flows by empowering you with greater data visibility and benchmark tracking.

One of the most obvious negative consequences of financial data silos between departments is that it reduces the cohesion of your corporate accounting department’s communications. This results in increased errors.

Analytics are increasingly used to optimize decision-making. As a result, companies that don’t adopt a unified system that produces comprehensive data sets can easily fall behind.

Treasury technology is quickly taking over as the foremost tool for liquidity management. So, let’s see how the use of data can optimize your CCC:

- **Improving Collections:** Accurate and up-to-date reporting on collectibles is critical for your receivables, as proactively addressing missing payments is impossible without knowing which payments are late. Technology can further assist collection efforts by automating reminders and offering predetermined incentives for early payments.
- **Increasing Float:** Float refers to the period during which transaction processing delays result in a double count of funds. More precise automated payment times can help you optimize your incoming cash flow to accrue interest or gain time before payments are processed.
- **Improving Operational Efficiency:** Thanks to the introduction of advanced digital treasury tools, paper or manual processing in AP or AR departments is quickly becoming a waste of time. Administrative work can be done more quickly and accurately by AI. Digital systems free your staff to work on more complex and goal-oriented issues like streamlining your CCC and reducing unnecessary expenses.

Data analytics is the future of financial decision-making, but many companies haven’t yet adopted an information-based approach. So, early system upgrades can potentially confer exceptional competitive advantages at the moment.

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5 STRENGTHEN RELATIONSHIPS WITH BANKS AND BANKING PARTNERS

Strengthening your relationship with your local bank is one of the most important (yet often overlooked) preparatory measures you should take in any economic climate, but especially if hard times are predicted.

Demonstrating your proactive liquidity management and holding early discussions about potential risks can build trust. It may even yield advantages such as favorable terms, reduced interest rates, and more capital.

The experienced banking partners at your local bank branch can be sound resources when you experience cash flow issues. Your bank wants to help you reach your financial goals, so you can get personalized expert advice on your unique situation. But first, you need to reach out and brief them on your company's strategies and finances.

Your local bank's liquidity management experts can help you set your industry benchmarks and implement tracking technology to measure your performance. They can also work with you set your finances in order. This includes granting you access to capital and helping you create a smart and strategic plan for optimizing operations.

Learning how to leverage new treasury technology can be intimidating, but a local financial partner can help you through the digital transition.

CONSULT WITH AN EXPERT TO OPTIMIZE YOUR LIQUIDITY MANAGEMENT

The five steps outlined in this article—improving visibility, establishing benchmarks, optimizing working capital management, unlocking trapped cash and strengthening your relationship with your local bank—are vital responses to volatile markets. Of course, they offer significant advantages even under normal circumstances.

The business world is going digital, making manual or paper systems obsolete. Upgrading your treasury systems enables both automated increases in efficiency and data analytics. What's more, optimizing your CCC requires extensive reporting capabilities within your system, so upgrading your processes is a competitive necessity.

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