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FINANCIAL FEED

2024.Q1

Fraud Trends and Best Practices

Tools and Resources to Help Fight Fraud

PAGE 14

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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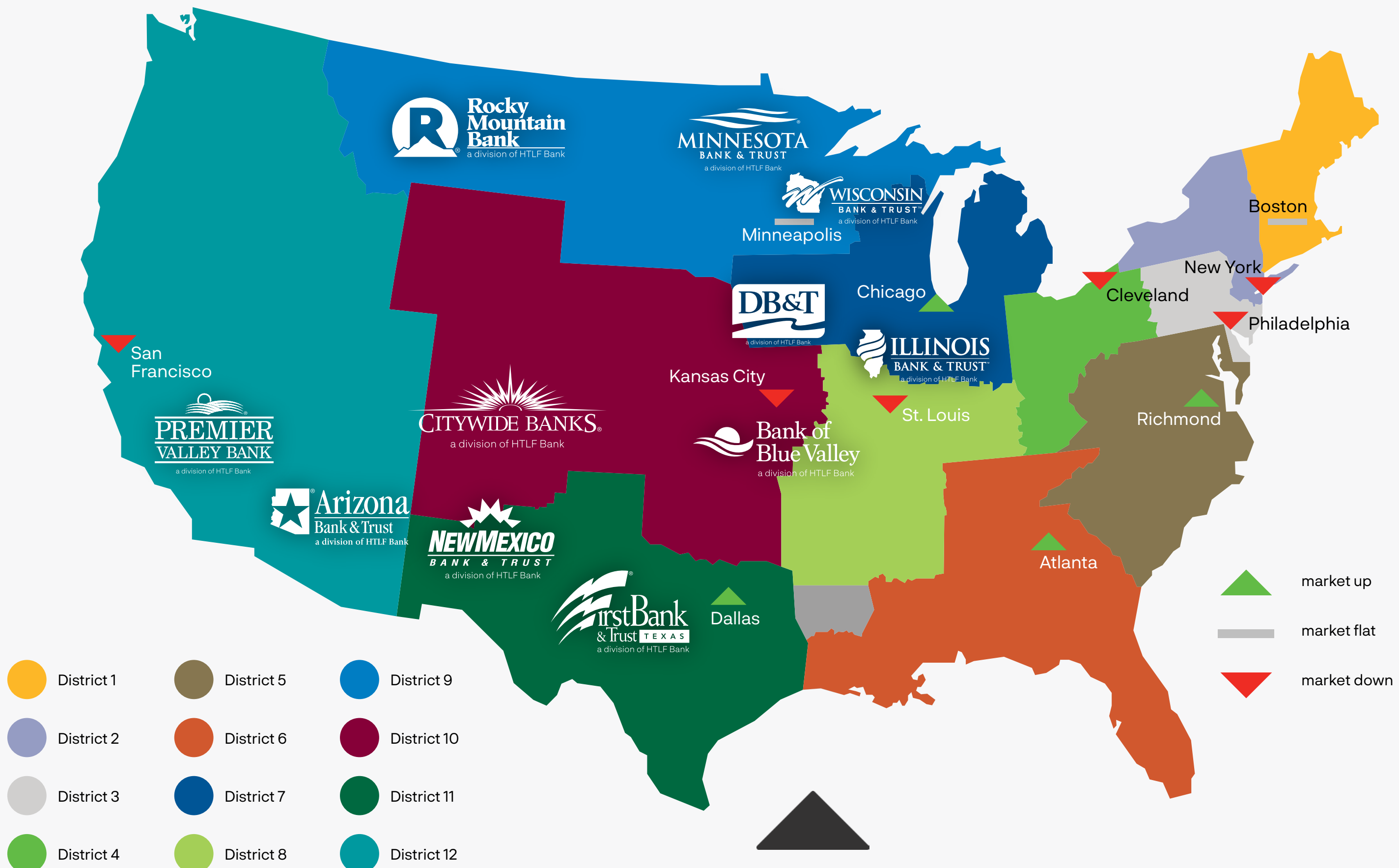
National Economic Activity

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 of 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.

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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 10th District

Previous softened economic activity leads to uncertainty

Economic activity in the Tenth District declined slightly in recent weeks. Consumers were increasingly likely to "share a roof and share meals" to manage household budget challenges. Demand for rental housing reportedly shifted away from single-bedroom units toward multi-bedroom housing where rent expenses could be shared with a roommate. Similarly, restaurateurs noted that revenues fell as more customers split dishes and eschewed expensive items. Manufacturing businesses reported little change in activity, though some contacts noted a decline in their expectations of demand over the medium term. Reports of planned capital expenditures were mixed depending on how directly businesses were supported by fiscal spending and municipal projects. Renewable energy activity in the Tenth District continued to expand at a moderate pace, driven by modest growth in wind generation and robust growth in solar installations. The outlook for renewable energy remained positive, but contacts noted skilled labor shortages and limitations on interregional electricity transmission as challenges. The agricultural economy and farm credit conditions in the District softened moderately.

Kansas is part of the 10th District of the Federal Reserve Bank.

LABOR MARKETS

Labor conditions in the Tenth District remained mostly unchanged over the past month. Hiring activity in the service sector was mixed across segments. Transportation contacts reported robust employment growth while most hotel contacts reported contractions in employment. Most contacts expected to increase hiring or maintain the size of their workforce over the next year, citing expected sales growth, overworked staff, and an ongoing need for workers with specific skills. Few businesses laid off workers, but many contacts reported reducing their workforce through natural attrition.

To build a skilled workforce, contacts noted raising wages for new hires, upskilling less-qualified workers, and making increased efforts to retain existing employees. Wages continued to grow at a moderate pace. Contacts highlighted raising wages as central to their retention of existing employees and attracting new hires over the past few years. However, some contacts noted an increased number of potential hires have refused the compensation packages offered, indicative of ongoing tightness in the labor market.

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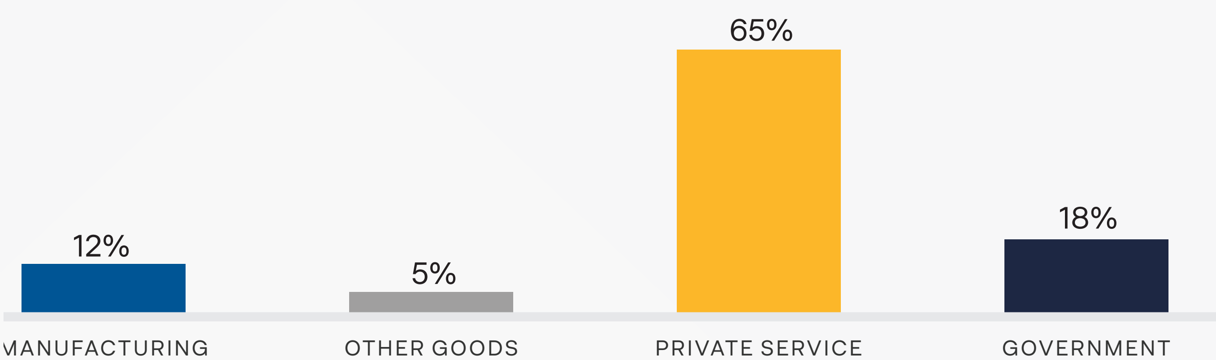
KANSAS

Employment Growth Rates

12-month percentage change, not seasonally adjusted

Source: FDIC State Profile



PRICES

Prices grew at a moderate pace. While manufacturing contacts witnessed a moderation in price pressures, service firms are still facing higher prices due to tight labor market conditions. Most firms reported plans to raise prices in coming months. Contacts reported concerns about risks of higher commodity and energy prices. While higher interest rates are raising financing costs for some companies, most District firms reported a majority of their funding coming from cash financing, insulating many District firms from the higher rate environment.

CONSUMER SPENDING

Consumer spending declined slightly in recent weeks. Contacts suggested consumers were increasingly likely to “share a roof and share meals” to manage household budget challenges. Specifically, contacts in multifamily housing reported demand for single-bedroom units softened, shifting toward demand for multiple bedrooms as more renters sought to share rent expenses with roommates. Restaurant owners similarly reported that, while patronage was steady, revenues fell as more customers shared plates and avoided higher cost items. Leisure travelers accounted for a smaller share of hotel stays.

MANUFACTURING AND OTHER BUSINESS ACTIVITY

Overall business activity declined slightly last month. Contacts in retail and tourism reported moderate declines in sales and revenues. Hoteliers reported occupancy levels remained steady but noted an increase in stays related to business travel. This shift in traveler type raised some concerns regarding future demand, as business travelers are reportedly more sensitive to price and business cycle fluctuations. Contacts in healthcare reported a somewhat lower outlook for use of services through the end of year. With greater enrollment in high-deductible health insurance plans in 2023, more households have yet to meet their deductible despite being late in the year and may forgo care requiring out-of-pocket payment. Manufacturing businesses reported little change in activity, though some contacts noted a decline in their expectations of demand over the medium term. Planned capital spending was mixed across segments with manufacturers reporting softening investment activity. Contacts noted the emergence of a firm-specific dichotomy whereby businesses that obtained government or defense contracts are fueling the majority of capital expenditure activity.

REAL ESTATE AND CONSTRUCTION

Several developers and construction managers reported raw materials costs stabilized recently. They also noted greater ability to push against escalating costs from subcontractors. Public sector funding for municipal projects sustained demand for building materials, somewhat supporting materials prices. Contacts indicated that subcontractors were becoming more available for work, with holes in their backlog schedules for the first time in several years. Though construction labor was somewhat more available, growth in labor costs remain elevated.

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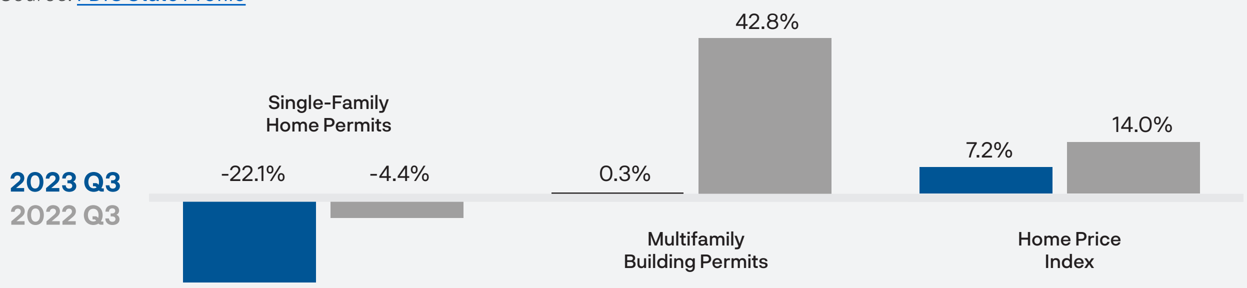
KANSAS

Other Economic Indicators

(not seasonally adjusted)

Source: FDIC State Profile



ENERGY

Renewable energy activity in the Tenth District continued to grow at a moderate pace, driven by modest growth in wind generation and robust growth in solar installations. Expectations were for a continued moderate pace of growth going into next year, driven mostly by wind generation. While growth in renewable energy in the District is expected to be slightly behind the U.S., Kansas and Missouri are slated to outpace the U.S. average in coming months. Contacts in the renewable energy sector highlighted acute skilled labor shortages and limitations on interregional electricity transmission as key challenges. While higher interest rates are adding to the renewable development costs, most of those higher costs are being passed onto consumers in the form of higher electricity rates. Contacts highlighted the significant boost to renewable development activity expected in the coming years from fiscal stimulus spending, equating that spending to “throwing gasoline on an already raging fire.”

Source: The Federal Reserve’s Beige Book

Outlook Across the 8th District

Previous softened economic activity leads to uncertainty

Economic activity in the Eighth District declined slightly since our previous reports. Labor markets remained tight but reports of easing continued. An increased share of contacts reported holding wages flat. Prices rose moderately, though businesses continued to report consumer price sensitivity. Retailers and freight transport contacts reported slowing demand, particularly for high-end goods, but hospitality and travel contacts saw steady growth. Construction activity slowed, especially for multifamily projects, many of which have been delayed or cancelled due to higher interest rates. Loan demand fell, and delinquencies ticked up above pre-pandemic rates. The general outlook for the regional economy weakened slightly due to concerns about future demand.

St. Louis is part of the 8th District of the Federal Reserve Bank.

LABOR MARKETS

Employment has remained unchanged since our previous report. Labor mismatches and struggles replacing departing employees have contributed to a tight labor market, but reports of easing have continued. Some contacts reported that availability of skilled workers remains a top issue, while others reported a more stable labor force for the first time in a few years. Staffing contacts reported clients are staying at jobs and less prone to leave than they were last year.

Wages have continued to grow slightly since our previous report, with an increased share of contacts reporting that wages remain level. A manufacturing contact in Evansville noted that hourly wages have risen only slightly, but an increase in overtime pay due to labor shortages has driven up labor costs. Several hiring contacts in St. Louis reported wage growth has slowed or reverted to pre-pandemic trends and fewer prospective employees have successfully negotiated for higher wages.

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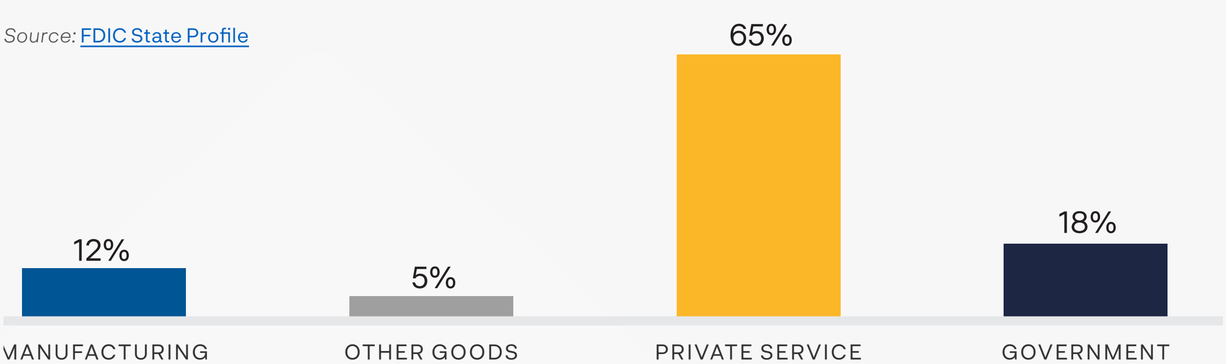
KANSAS

Employment Growth Rates

12-month percentage change, not seasonally adjusted

Source: FDIC State Profile



PRICES

Prices have increased modestly since our previous report. Although approximately three-quarters of contacts reported higher labor and nonlabor input costs, many businesses are choosing to maintain or only slightly increase prices. Among respondents who do not plan to fully pass on costs to consumers, two main reasons stood out: First, some previous price increases were enough to cover more-recent cost increases. In an effort to raise prices less frequently, some businesses hedged by implementing larger increases earlier in the year. For example, an Arkansas brewer reported that they incorporated potential future volatility in input costs in past price increases. Second, increased consumer sensitivity to price increases has lessened businesses' ability to raise prices. Some items, such as luxury handbags and watches, have seen price decreases of about 15%.

CONSUMER SPENDING

District general retailers, restaurant, and hospitality contacts reported mixed business activity since our previous report. In general, auto dealers reported a decline in business activity. Louisville auto contacts reported that higher interest rates have slowed consumer demand for new car purchases. October real sales tax collections increased in Kentucky, Missouri, and Western Tennessee relative to September and decreased in Arkansas. A Little Rock pawn shop noted that, while sales over the past 18 months have been at high volumes historically, sales have slowed in recent months. A Memphis hospitality contact noted that hotel occupancy rates have been consistent compared with the same 6-month period last year.

MANUFACTURING AND OTHER BUSINESS ACTIVITY

Manufacturing activity growth has declined slightly since our previous report. In Arkansas and Missouri, firms reported slight decreases in production and employment and slight increases in delivery lead times and new orders. Missouri reported a slight decrease in inventories, while Arkansas saw a very slight increase. Higher interest rates and the auto worker strikes impacted deliveries of some products for local automotive markets. On average, firms reported they expect slight decreases in production, capacity utilization, and new orders in the coming quarter.

NONFINANCIAL SERVICES

Activity in the nonfinancial services sector has cooled since our previous report. Overall, sales and sales expectations were the same or slightly lower, and the general outlook was slightly worse. A Louisville tourism contact reported postponing capital expenditures because of flagging demand but also reported local growth in the hospitality industry. A St. Louis tourism contact reported continued investment and expressed hope that the local economy would be somewhat insulated from economic challenges faced by more expensive areas. A Memphis freight contact echoed the sentiment of low demand, which, coupled with overbuying during the COVID pandemic, has contributed to slow reduction of inventory. A St. Louis transportation contact reported stable demand from ongoing customers, but less new client acquisition. A Little Rock healthcare provider reported lower sales expectations and a worsening outlook.

REAL ESTATE AND CONSTRUCTION

Residential rental prices across the District have remained unchanged since our previous report. In the Louisville, Memphis, and Little Rock MSAs, pending sales and houses off the market in two weeks have fallen since our previous report, while inventory and months of supply for residential real estate have increased. Contacts reported high mortgage rates continuing to constrain demand for buying homes. In commercial real estate, strong demand for office space continues to be focused on Class A buildings, while vacancies remain high for Class B and C office space.

Commercial construction has slowed sharply since our previous report, particularly for new starts in the warehouse and industrial sectors. Residential construction has also seen slowing activity, with some projects sidelined or cancelled, especially for multifamily. One Memphis commercial real estate contact reported that new construction has all but stopped for developments aside from single-family housing. While the number of ongoing projects remains high, contacts with a strong existing project pipeline have reported slowing demand for future projects.

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AGRICULTURE AND NATURAL RESOURCES

Agriculture conditions have improved slightly since our previous report. Yields for the District's primary commodity crops were at or moderately below 2022 levels. Despite this slight decline, total corn production in the District rose relative to last year. Rice production also rose, reaching levels over 33% higher than in 2022, while soybean production dipped slightly below 2021-22 levels and cotton production returned to 2021 levels. Commodity crop prices fell but remained at or above typical levels for the 2015-2020 period and stayed relatively stable throughout the reporting period. District contacts reported a mixed outlook but were generally less pessimistic than in previous reports. A Louisville contact attributed the moderate improvement in outlook to higher-than-expected yields and prices for crops such as corn and soybeans.

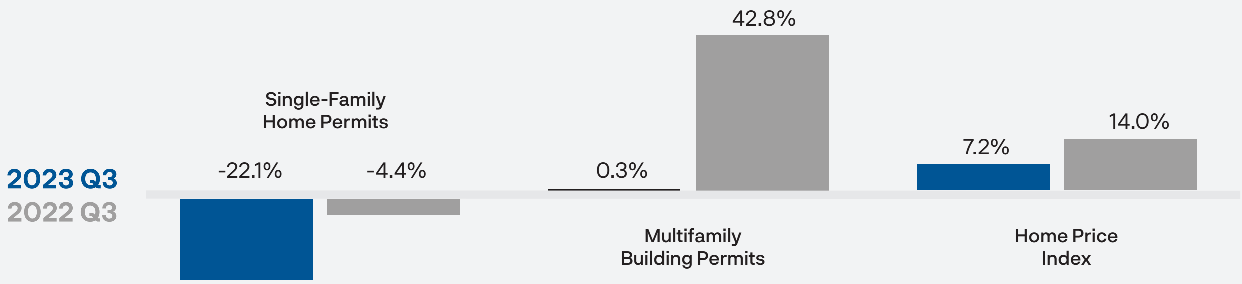
District contacts reported a mixed outlook but were generally less pessimistic than in previous reports.

KANSAS

Other Economic Indicators

(not seasonally adjusted)

Source: FDIC State Profile



Source: The Federal Reserve's Beige Book

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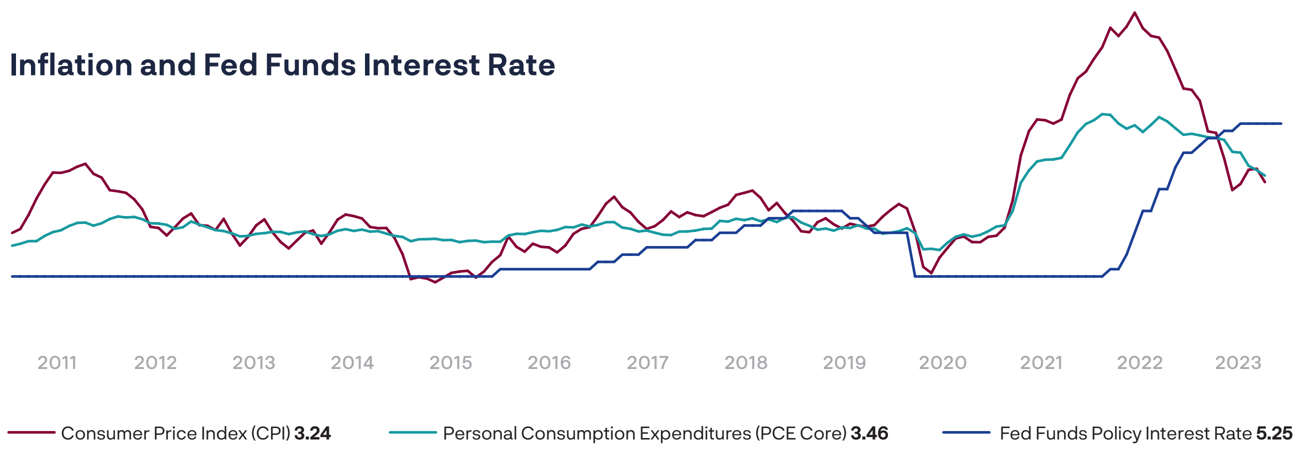
The Recession of 2024 Might Surprise Everyone

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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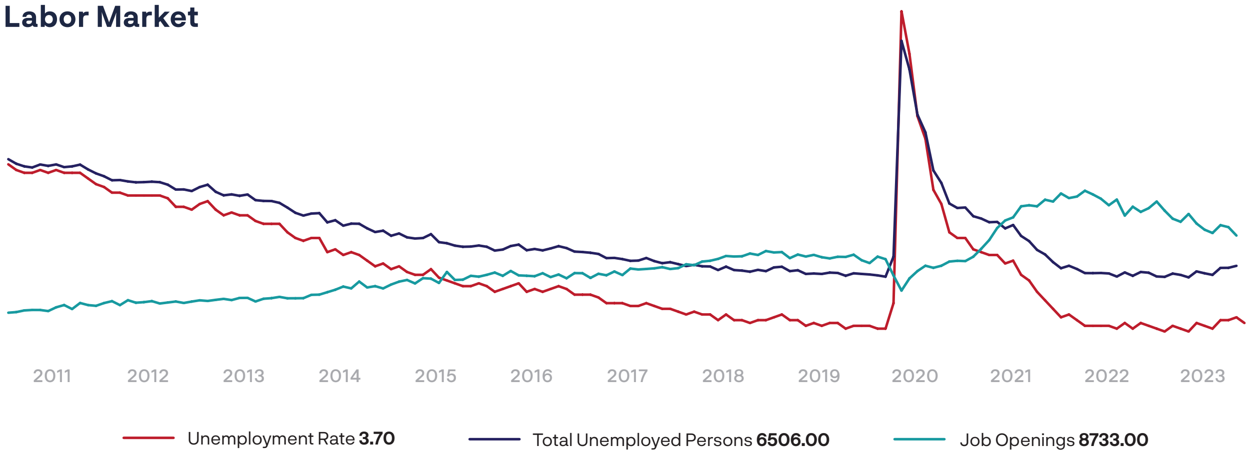
Labor Market



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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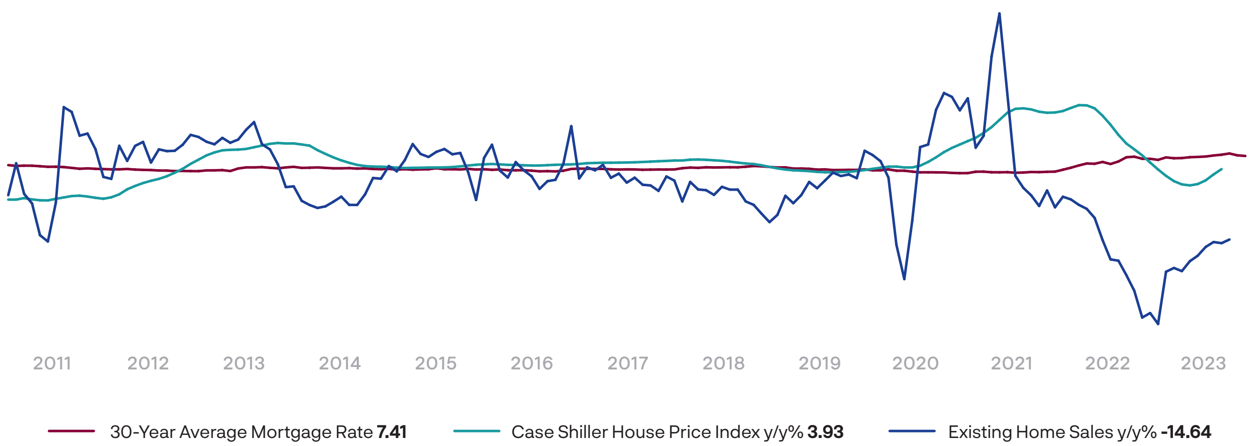
Housing Market



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 Bank of Blue Valley, 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 accounts receivable (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 get 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.

The experts at Bank of Blue Valley, a division of HTLF Bank, are here to help you **increase your financial performance** by **optimizing your cash flow and increasing your access to working capital.** They can help you strategize for future uncertainties and shore up your company's financial health.

Scan here to get help strategizing for future uncertainties and shore up your company's financial health with your banking partner today!

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