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a division of HTLF Bank

FINANCIAL FEED 2024.Q1

Fraud Trends and Best Practices

Tools and Resources to Help Fight Fraud

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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Optimize capital, streamline cash management, fight fraud with Positive Pay and more – all with one comprehensive solution.



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HTLF Bank is MEMBER FDIC and  EQUAL HOUSING LENDER

A Message from Doug Kohlbeck

Banking partners you can count on to help you achieve growth goals

Wisconsin's strong manufacturing economy is expected to remain solid in 2024 as businesses focus on increasing margins that took a hit during COVID and the following years.

Starting in 2022 and throughout 2023, there was a pullback of capital investment. The level of expansion, new equipment, and growth investments was tepid.

While companies, post-Covid, are focused on driving up their returns from the investments they made in 2021 and 2022, that should not hold back manufacturing in 2024.

"We're also seeing a normalization of inflationary pressures, which will also help boost margins," Doug Kohlbeck, President and CEO of Wisconsin Bank & Trust, a division of HTLF Bank, said.

The bank's portfolio is 65 percent commercial and industrial, 15 percent production agriculture, 20 percent commercial real estate.

MARKET ADVANTAGES

Kohlbeck has enthusiasm going into the new year due, in part, to the reduction in supply chain issues and labor issues have improved.

"What we're hearing from our customers is they're now getting stronger candidate pools for their openings. There are companies adding new and better talent," Kohlbeck said.

"What we're hearing from our customers is they're now getting stronger candidate pools for their openings. There are companies adding new and better talent."

Doug Kohlbeck
President & CEO



Some of those companies are using stronger candidates to replace less productive workers they hired when the labor market was tighter.

Better talent means labor costs continue to rise.

"You've got to pay a lot for good, quality talent and I don't see that stopping," he said.

MARKET CHALLENGES

There are a few challenges for service industries to highlight going into 2024. With low housing supply, high interest rates, and increased construction costs, this market has a few obstacles to overcome this year.

While job cuts in that sector will improve 2024 budgets, sales of new units are extremely low due to the cost of construction. Rates are driving this trend.

"A lot of multifamily construction was done in 2022, but not a lot of new projects started in 2023. So, we're going to hit a little lull here in terms of housing units coming online, particularly in the multifamily," he shares.

As Wisconsin faces affordability issues seen in many places nationwide, rental rates of the new multifamily are at much higher levels because home ownership is harder.

"At least for the foreseeable future, our housing environment is going to be kind of stuck," Kohlbeck summarized.

WHAT YOU CAN DO

Let's talk about inflation.

"Any nonservice company in our portfolio has either recently invested or plans to invest in more technology-driven automation whether it's robotics or taking out steps in their production lines," shares Kohlbeck.

A company that makes building supplies has gone all in on robotics. They're still maintaining a manual line until they can work out production, but it would take them 13 people to do the work of two people plus the robots.

“We encourage our clients to bring in that historical data for context when evaluating their current state. What impacts are they seeing? What strategies have they employed? What is their current plan? We listen, learn, and offer strategic insights based on our client’s unique situations.”

- Doug Kohlbeck , President & CEO

There’s a significant cost savings and they can produce more products faster through robotics. Companies that do not make these changes have had to transition to what Kohlbeck calls a specialized business. These are shorter run manufacturing companies that take on harder projects with harder engineering in order to bring in higher revenue and support labor costs.

Kohlbeck highly recommends businesses have a recession contingency plan.

“If we were to enter a shallow or deep recession and if that persisted for a while, what would those indicators be? How would your businesses respond to that? We really still don’t know where this economy is going. Is networking part of your strategy? What is your peer group saying? These are questions that I believe companies should consider to be prepared,” he said.

It’s also important for your business to have foresight into your projected pipeline.

“You don’t want to get caught flat-footed,” Kohlbeck explains, “You need to understand if your cash-flow cycle is short, medium or long and then zero in on demand.”

Manufacturing is holding up well, considering all of the factors in play. In other industry pockets, there are companies that aren’t as fortunate.

“If your company’s margins don’t bounce back in 2024, I encourage you to investigate why, then manage changes to get the company back to an acceptable return,” Kohlbeck recommends.

HOW WE CAN HELP

The bank can help with that investigation.

“This is an everyday discussion internally and externally. Almost every company I see has lower gross margins in 2023 versus prior years,” Kohlbeck said.

When the bankers reviewed similar numbers from 2019, the stories they told were very different. The pandemic years brought stimulus payments, supply

chain issues, and an entirely new host of issues for companies.

“We encourage our clients to bring in that historical data for context when evaluating their current state. What impacts are they seeing? What strategies have they employed? What is their current plan? We listen, learn, and offer strategic insights based on our client’s unique situations.”

Then there’s fraud – an issue that’s not going away.

“There are small-to-medium companies that do not fully understand their risk from fraud,” Kohlbeck said.

“It’s still surprising to me how many of these companies have checks as their primary transactions. That’s not best practice for security reasons,” he said.

Cyber risk is also a concern.

“I don’t think the owners really understand how easily their systems could be exposed,” he said.

The bank has a very strong Commercial Card program that alleviates this pain point.

“Our Commercial Card remains the safest transaction form,” he asserts.

The Commercial Card and Treasury Management not only fight fraud, but they also allow customers to extend their cash flow.”

The Commercial Card is only one part of the value that the bank offers. With individual support, market insights, and fraud detection, Wisconsin Bank and Trust has provided a comprehensive solution for business needs.

“We’re unique. You don’t see a lot of banks our size offer this kind of Commercial Card,” he said.

If companies still want to write checks, we also offer Positive Pay, enabling customers to review account numbers, check amounts, and payee names before the bank processes the check.

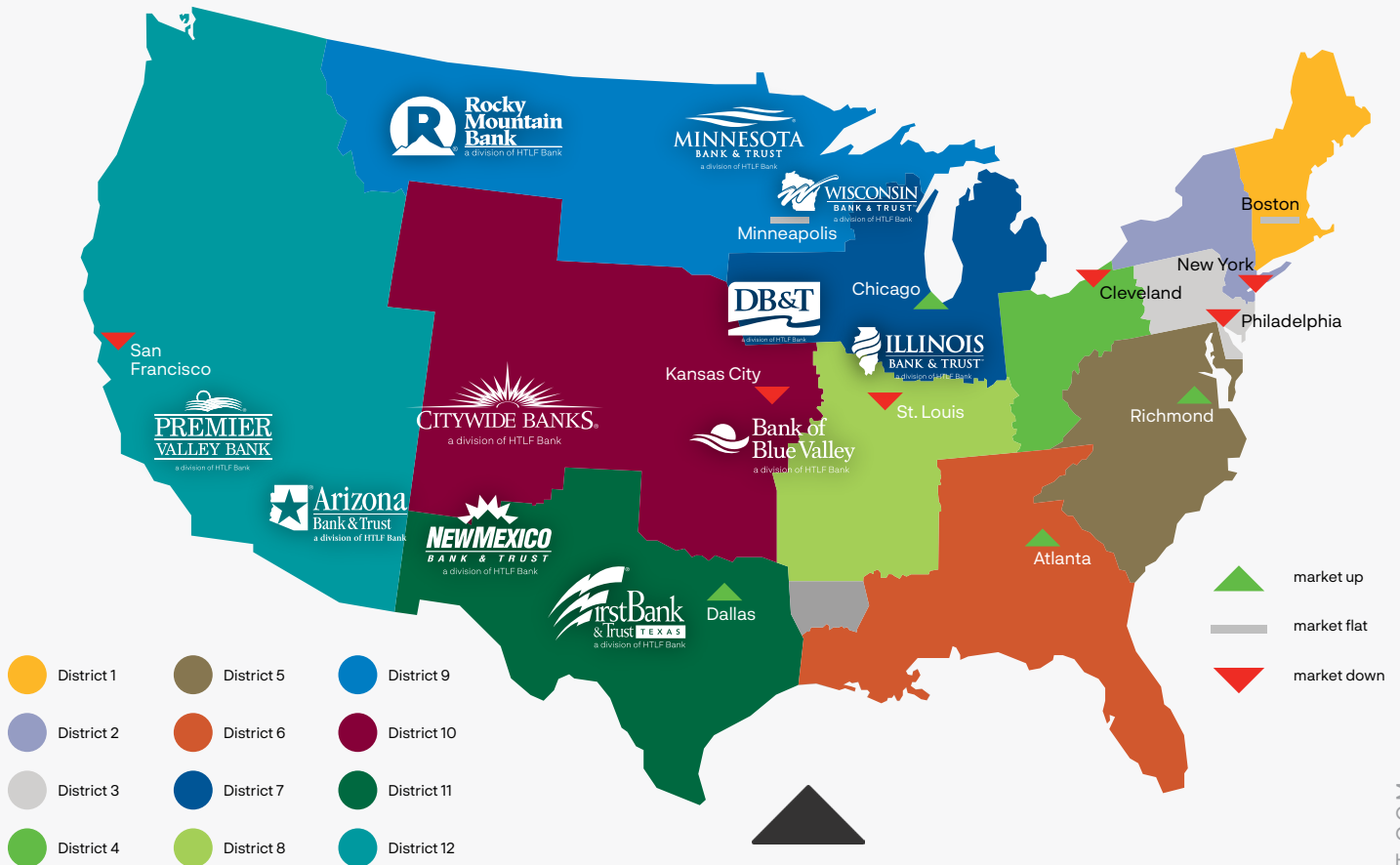
We put the client at the center of everything we do. We’re here to help your business grow. ▲

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 7th District

Previous softened economic activity leads to uncertainty

Economic activity in the Seventh District was up slightly overall in October and early November.

Contacts generally expected a small decline in demand over the next year and many continued to express concerns about the potential for a recession. Employment increased moderately; business spending was up slightly; nonbusiness contacts saw little change in activity; consumer spending and construction and real estate activity decreased slightly; and manufacturing was down modestly. Prices and wages rose moderately, while financial conditions tightened slightly. Expectations for farm incomes in 2023 were little changed.

Wisconsin is part of the 7th District of the Federal Reserve Bank.

LABOR MARKETS

Employment rose moderately over the reporting period and contacts expected a similar rate of increase over the next 12 months. Some manufacturers continued to have difficulty finding workers, particularly higher skilled ones. However, there were also signs that the labor market was cooling. Some contacts said their applicant pools had grown and that turnover had declined. And some contacts in construction, real estate, and finance reported taking down job postings, while others in those sectors were planning for layoffs.

PRICES

Prices rose moderately in October and early November and contacts expected a similar rate of increase over the next 12 months. Nonlabor costs were up moderately, in part because of increases in energy and shipping costs. Some contacts noted that while they had fewer supply chain issues, raw materials remained expensive. A few producers said that they were getting more pushback on price increases. Consumer prices moved up moderately due to solid demand and the passthrough of higher costs.

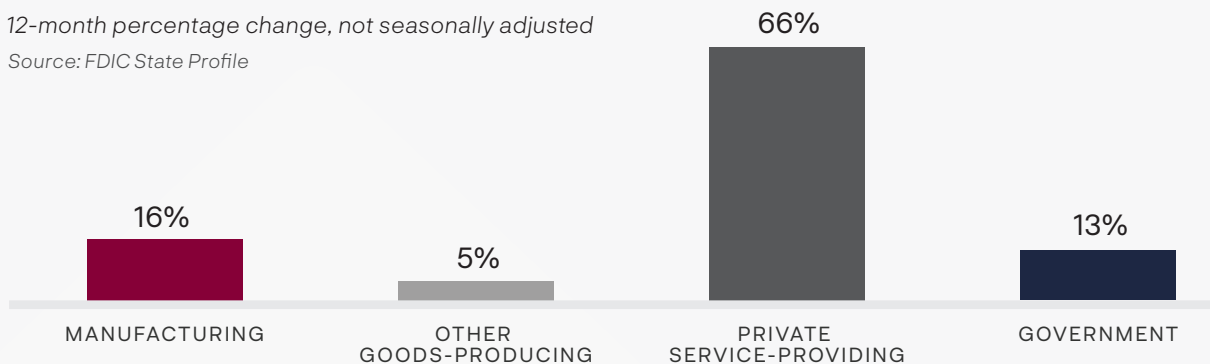
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Employment Growth Rates

12-month percentage change, not seasonally adjusted

Source: FDIC State Profile



CONSUMER SPENDING

Consumer spending decreased slightly on balance over the reporting period. Nonauto retail spending was up slightly. Contacts highlighted higher spending on luxury items, new product lines, lower-priced items at outlet stores, and at e-commerce websites. However, a processor of product returns reported that returns of clothing and electronics were down, which is an indicator of lower sales of those items. In the leisure and hospitality sector, spending fell on air travel and hotels. Light vehicle sales decreased modestly overall. New vehicle sales were down but held up better than expected in light of the UAW strike, with several dealers commenting they saw little effect from the strike. Used vehicle sales fell. Contacts noted that lower-end used vehicles were selling faster than higher-end models.

BUSINESS SPENDING

Business spending increased slightly in October and early November. Capital expenditures moved up slightly, with several contacts reporting purchases of new software. That said, a number of contacts said higher interest rates and tighter lending standards were leading them to hold off on investments until credit conditions loosen. Demand for heavy truck transportation services declined moderately. Residential and commercial electricity usage decreased modestly, but industrial electricity consumption was up some, with one contact noting an increase after the end of the UAW strike. Inventories for most retailers were near desired levels. According to contacts, the UAW strike had little effect on overall auto inventories. In manufacturing, inventories were generally a little high. Most contacts noted fewer input shortages overall, though some remained, including for specialty electrical and polymer components.

▲ A number of contacts said higher interest rates and tighter lending standards were leading them to hold off on investments until credit conditions loosen.

CONSTRUCTION AND REAL ESTATE

Construction and real estate activity decreased slightly on net over the reporting period. Residential construction was down slightly with demand for major remodeling projects falling substantially. According to a survey, homebuilders were more pessimistic about activity in the coming months than they had been earlier in the year. Residential real estate sales decreased slightly, while continued low home inventories supported a slight increase in prices and rents. Nonresidential construction activity was unchanged as were prices of new construction. Contacts again reported that high interest rates were forcing previously financially viable projects to be delayed indefinitely. Commercial real estate activity declined slightly, though vacancy rates and the availability of sublease space also fell. Prices and rents edged down. One contact reported that while leasing activity had held up, sales activity had fallen off.

CONTINUED ON PAGE 9

The payments landscape is changing.

With 73% of companies transitioning from paper checks to electronic payments¹, now is the time to make the switch from outdated, costly and time-consuming payment methods.



¹2022 Association for Financial Professionals
Payments Cost Benchmarking Survey

Scan here to learn more about the
Commercial One Card or stop by one
of our banking centers.



MANUFACTURING

Manufacturing demand decreased modestly overall. Steel and fabricated metals orders ticked down, with contacts highlighting lower sales to the construction, automotive, and medical sectors. Machinery sales were down modestly, in part because of fewer sales to the automotive sector. Auto production declined on average over the reporting period, largely because of the UAW strike. Heavy truck demand decreased modestly.

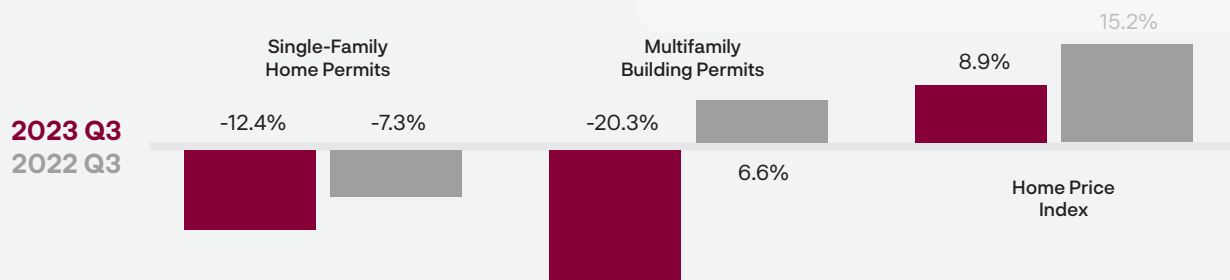
▲ Auto production declined on average over the reporting period, largely because of the UAW strike.

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Other Economic Indicators

(not seasonally adjusted)

Source: FDIC State Profile



▲ Despite widespread drought, there were reports of record yields across multiple states and crop types, including corn, soybeans, tomatoes, and wheat.

AGRICULTURE

Projected farm income in the District was little changed over the reporting period as both expenses and expected revenues moved lower. Despite widespread drought, there were reports of record yields across multiple states and crop types, including corn, soybeans, tomatoes, and wheat. One contact mentioned that early and dry spring planting contributed to better-than-expected crop yields. Corn and soybean prices dropped to their lowest levels in over two years, while wheat prices were flat. Costs were lower for key crop inputs, including fuel and fertilizer. Egg prices edged up, milk prices were flat, and butter prices were down. Cattle and hog prices both declined.

Source: The Federal Reserve's Beige Book

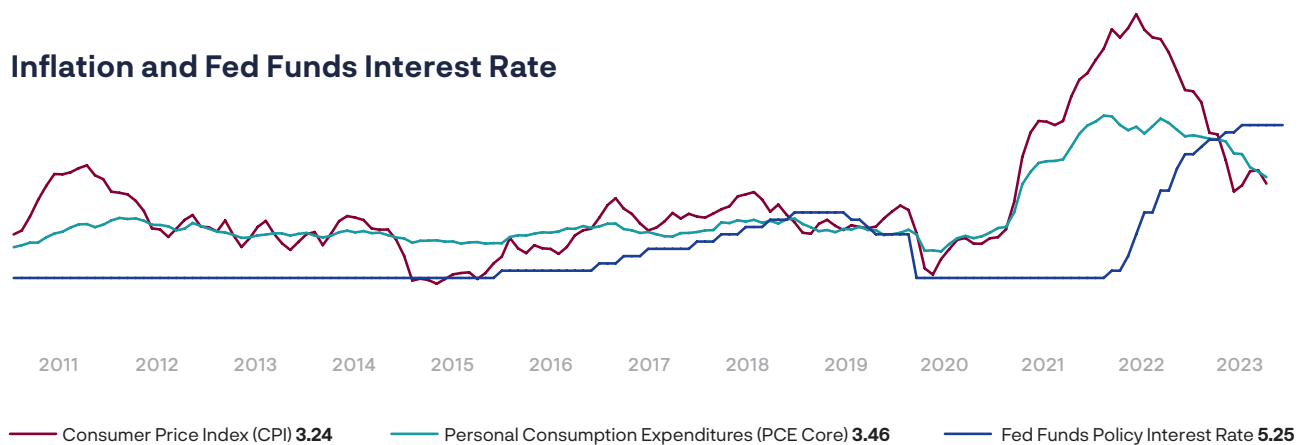
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The Recession of 2024 Might Surprise Everyone

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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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.

LOOKING FOR SLACK IN THE LABOR MARKET

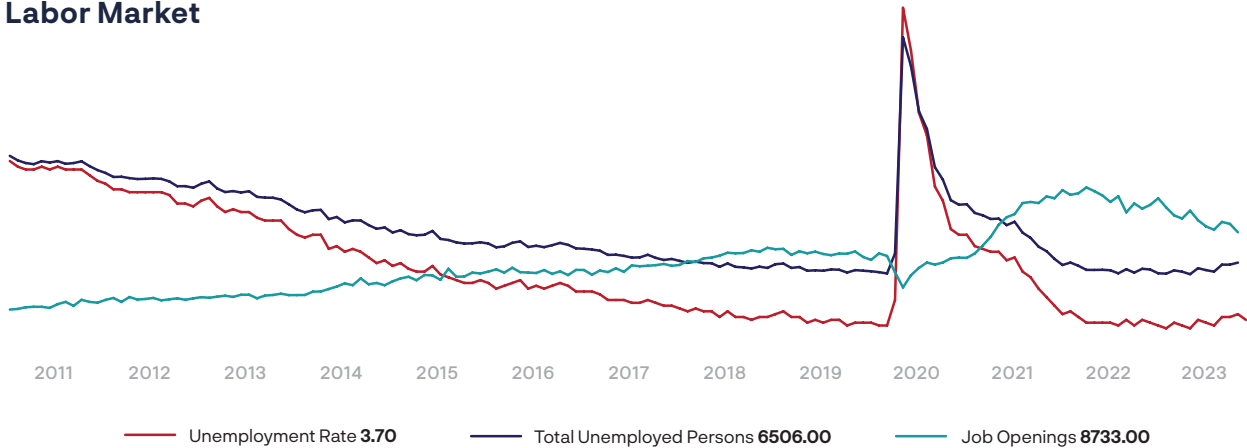
The unemployment rate hit a 50-year low at the end of 2022.

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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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.

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.



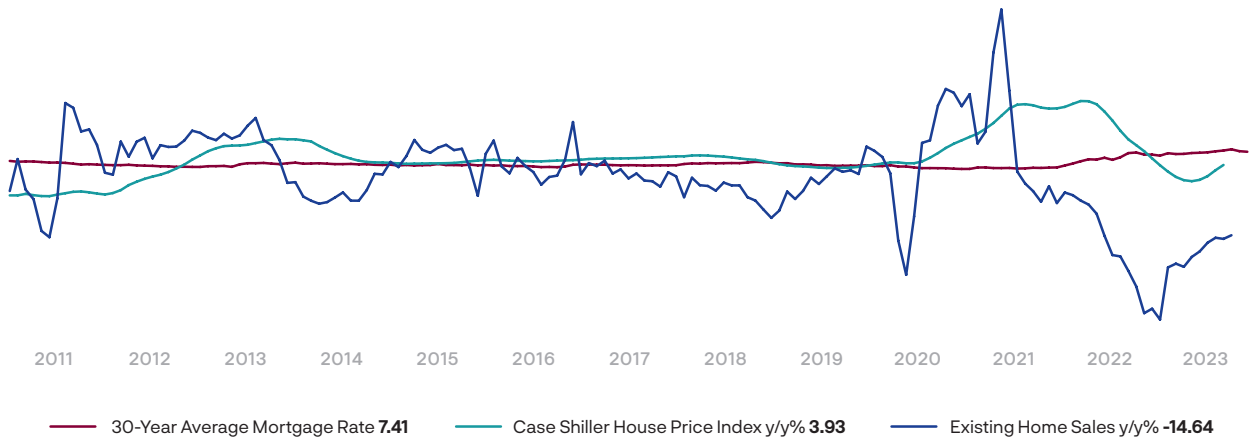
Paul Dickson
Director of Research, VP

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.

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.

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%
WIRE TRANSFERS



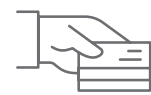
34%
ACH CREDITS



26%
ACH DEBITS



16%
CHECKS



8%
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](#)

All Pertinent Disclaimers: As with all serious financial topics or decisions, be sure to consult with a trusted financial advisor beforehand. The content here is for educational purposes only and is not meant to serve as any sort of advice or endorsement.



Contact Wisconsin 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.

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. ▲

The experts at Wisconsin Bank & Trust, 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.



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² Average cost savings are calculated based on the per-item costs detailed in the Treasury Management Fee Schedule for all services included in Business Bundle Plus. Average cost savings are calculated based on the \$75.00 Business Bundle Plus fee being waived for 12 months. \$75.00 Business Bundle Plus fee can be waived for customers with an average relationship balance of \$75,000. The balance threshold tied to the bundle waiver is the average book balance of a non-interest-bearing checking account with primary account ownership. New Business Bundle Plus enrollments will not incur Business Bundle Plus fee for the initial six-month period. Customers will be responsible for all service fees after this initial period, as outlined in the service agreement. Advanced Business Checking Account or Public Funds – Advanced Business Checking Account is required to enroll in the Business Bundle Plus.



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