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**FEATURE** | MONDAY, APRIL 19, 2010

# My, What a Nice Stash of Cash

By **LAWRENCE C. STRAUSS**

*Goodyear and Whirlpool are among the many companies that boosted cash flow through accounting maneuvers. For some, it may backfire.*

**AMID LAST YEAR'S WRENCHING ECONOMIC** downturn, many U.S. companies increased their cash positions to shore up their balance sheets.

No surprise there. But part of the build-up in cash had nothing to do with selling more goods or services. Instead, lots of companies made adjustments to their working capital, which is the difference between a company's current assets and liabilities, excluding cash and short-term borrowing. Typical moves included reducing inventories, taking more time to pay bills and inducing customers to pay their bills faster, thus reducing accounts receivable.



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Dan Picasso for *Barron's*

**Fortune Brands** (FO), **Whirlpool** (WHR) and **Goodyear Tire & Rubber** (GT) are among the companies whose operating cash flow benefited from such steps, all of which are fully allowable under generally accepted accounting principles, or GAAP. Fortune Brands stretched out its payments to vendors, as did Whirlpool, which also cut its inventory. Goodyear, too, reduced its inventory -- by about \$1.1 billion -- even as its receivables fell, giving a big boost to operating cash flow.

While all three companies have solid finances, such moves raise eyebrows for some analysts and investors, and could influence stock-market valuations. Adjustments to operating leverage have delivered a one-time boost for many companies, says Will Becker, a securities analyst at Behind the Numbers, a Dallas firm that specializes in accounting research.

The problem, he says, is that "once that card has been played, there is no encore."

Becker recently identified 173 S&P 500 companies that had boosted their 2009 operating cash flow via working-capital adjustments. He worries that, when the economy rebounds fully, they will use a lot of cash to replenish inventories, potentially crimping their free cash flow. That is what is left over once a company has made the necessary investments in its operations. Free cash can be used for share buybacks and dividends, among other value-enhancing measures.

Jeff M. Fettig, chief executive of Whirlpool, addressed working-capital issues in the company's fourth-quarter conference call earlier this year. Working capital was a source of cash for Whirlpool in 2009, due in part to its slashing inventories about 15%, to just under \$2.2 billion. At the same time, accounts payable climbed 18%, to \$3.3 billion. These moves "significantly improved our financial and liquidity positions," Fettig said.

This year, however, Whirlpool expects to consume cash "as we return to sales growth," Fettig told analysts.

Jeffrey Coons, co-director of research at Manning & Napier, a Rochester, N.Y., asset manager with a value focus, notes that working-capital modifications generally are one-time measures, or at least short-lived. "There are a handful of companies with the financial strength and market-share clout to manipulate working capital as a bridge until top-line growth resumes," he says.

#### **Table: Stretching Their Dollars**

Whirlpool's revenue fell 9.5% last year, and Fortune Brands' declined 12%. Goodyear's sales were off 16%, to \$16.3 billion; the company posted a loss of \$1.55 a share.

**FORTUNE BRANDS, A MINI-CONGLOMERATE** that sells spirits, cabinetry and golf products, improved its 2009 operating cash flow in part by allowing accounts payable to climb by \$90 million. "None of the working-capital changes that occurred in 2009 will impact our financial flexibility in future periods," says a company spokesman. "We feel very good about our prospects for achieving our free-cash-flow target in 2010."

When it comes to valuing stocks, cash flow matters. "The business' value is the present value of expected future discretionary cash flows," says Wally Weitz, president of Wallace R. Weitz, an Omaha asset manager. "Changes in working capital are important to know," he says, especially if they are more than mere noise that fluctuates with the business cycle.

In Goodyear's case, adjustments to working capital accounted for more than 80% of last year's \$1.3 billion in net cash from operations. "Given the difficult economic environment and the uncertainty in the capital markets, we took several actions to strengthen our liquidity in 2009, including strong working-capital management," the company noted in its 2009 10K filing.

#### *The Bottom Line*

Behind the Numbers, a firm that analyzes accounting, recently counted 173 S&P 500

But, as Chief Financial Officer Darren Wells said in Goodyear's most recent conference call in February, one of the challenges now will be "to constrain

companies that boosted their 2009 operating cash flow via working-capital adjustments.

working-capital growth as volumes increase and raw-material costs drive higher inventory and receivable

values."

On the same call, Richard Kramer, then chief operating officer and now CEO, insisted Goodyear could expand its business "without substantially growing our inventory...on a unit basis."

Still, Coons of Manning & Napier worries that some companies eventually will be hurt by working-capital decisions, especially if revenue doesn't grow as expected. After all, the remedy won't work forever.

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