# Introduction

A central theme for cash-flow statements is current-period income can differ significantly from current-period cash flows and both measures have important consequences for future cash flows.

To see what we mean here, consider the financial value of your human capital–your future earnings power. It is by far your biggest asset even though banks and other lenders would not allow you to recognize it on your balance sheet because it can't be measured reliably. Likewise, they would not allow you to recognize the increases in the value of your human capital on your income statements; however, from an economic perspective it is probably by far the biggest source of income you earn while in college. Thus, by performing well in school this term you earn current income by increasing your human capital; thus, increasing your future earnings power and future cash flows. However, you need current cash flows for tuition, books, etc. Indeed, students often generate a great deal of income while in college, but continually run out of cash and confront liquidity crises.

Like you, most companies have significant differences between current-period income and current-period cash flows. For instance, Intel reported nearly $13 billion of net income during fiscal 2011, which was significantly less than the nearly $21 billion of net cash inflows from operating activities. Net income is an important measure of Intel's performance during 2011; however, an analysis of Intel's cash flows can provide additional information needed for forecasting future performance.

By the end of this chapter, you'll understand how Intel's cash-flow statements, and those of other companies, help analysts gain insights into current and future performance. Such cash flow analyses are increasingly important during tight credit markets, as they were during the financial crisis of 2007-2009.

Cash-flow statements have two functions: (1) they help users predict future cash flows by explaining the current-period change in cash in terms of operating, investing, and financing business activities, and (2) they help users reconcile differences between net income and net cash from operating activities, which helps them assess the quality of net income and predict when income will be converted to cash.

**Operating cash flows** mostly pertain to ongoing activities that support a company's primary business purpose including events associated with research and development, purchasing, manufacturing, sales, marketing, distribution, customer collections, and support.

**Investing cash flows** are primarily associated with buying or selling property, plant, and equipment, intangibles, and most types of investment securities. They also include cash flows associated with buying or selling complete companies.

**Financing cash flows** primarily result from transactions with owners (e.g., dividend distributions, stock issues, and stock repurchases), issuing debt, and repaying debt principal.

With regards to cash-flow statements, GAAP defines operating activities as a residual concept to include all activities that do not meet the criteria to be classified as investing or financing activities. As a result, cash from operating activities also includes a few items that seem to have very little to do with operating activities such as income tax payments.