Intrawest Faces Steep Slope To Reach Cash Flow Targets

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Intrawest shares were already climbing something of a steep peak before investors heard the good news that Vancouver will host the 2010 winter Olympics. After yesterday's burst of energy, they're closer to the top -- or to the precipice.

It's hard to see how millions worth of free improvements (thank you, taxpayer) won't help the company's fortunes, but let's be realistic: Whistler-Blackcomb may be the company's crown jewel, but it's nonetheless a small part of the overall business. And the Olympics are seven years away. A quick and judicious short sale would have been just the thing as the buying hit a high pitch yesterday.

Beyond all the excitement, there seem to be both problems and opportunities at Intrawest. It owns some good properties, some of which aren't fully developed, suggesting that there's room for growth. And we all know the demographic argument about aging baby boomers.

But the company itself believed a little too ardently in its prospects as it cobbled together its suite of assets in the nineties. The money didn't flow quite as fast as expected, and the balance sheet suffered as debt balances swelled. SARS and wars didn't help.

The upshot is that Intrawest had to lower its guidance the last time it produced quarterly numbers, in mid-May. Given that the upside for today's investor depends on the company's ability to pay down debt, that was unfortunate. But it didn't stop management from putting on a brave face: "We remain on track to achieve our goal of significant free cash flow and debt reduction in fiscal 2004," CEO Joe Houssian said.
The stock got crushed, but as we know, it's back in the black today.

To assess the realism of the company's stated goal, we check in with **Veritas Investment Research**, since the boutique predicted that the company would miss its 2003 forecasts in April. The verdict is a little sobering for investors bidding up the stock.

Intrawest's 2004 goals are for free cash flow of between $250-million and $270-million, which could be partly applied to debt repayments. That could lighten the debt burden to $780-million from $960-million and trim the debt-to-EBITDA (earnings before interest, taxes, depreciation and amortization) ratio to about 2.7 times. It's a high 4.6 times now.

The trouble, as the analysts see it, is that free cash flow at Intrawest has been as common as a monkey on skis. Consolidated free cash flow has been negative since 1998. Much of the cash burn, it should be said, stems from the real estate development operations, which the company has hived off into joint ventures. But **Veritas**' Patrick Stephenson and **Anthony Scilipoti** figure the ski and resort side of the business have also been a drain.

The conclusion, then, is that the company's free cash flow estimate includes land sales and relies on a turnaround at the resorts and on the hills. That doesn't look more likely today than it did in April. And although including land sales in free cash flow doesn't alter the possibility of paying down debts, investors should be wary about considering real estate sales as free cash flow, since they're not a recurring income stream.

In some ways -- price-to-book and perhaps price-to-earnings, for instance -- Intrawest might look cheap. But as has been chronicled at length before, the company's accounting earnings, given the nature of the business, are not of the highest quality. Cash flow is the answer, but it's fraught with pitfalls of its own.

Intrawest's Numbers
(Amounts in thousands of U.S. dollars)

Assets	
Cash and equivalents	$85,222
Total current assets	$864,841
Ski/resort operations	$870,567
Properties	$572,407
Other long term assets	$1,017,020
Total assets	$2,414,994
Liabilities	
Bank and other debt	$246,941
Total current liabilities	$582,644
Long term debt	$946,196
Other long term liabilities	$170,916
Total liabilities	$1,699,756
Equity	$715,238