

# Free Cash Flow

Free cash flow is essentially cash profits (profits that result when any accruals and estimates are stripped from the numbers) reduced by cash investments or capital expenditures.

One simple method to calculate free cash flow is to simply add cash flow from operations to cash flow from investing. Cash flow from investing is usually a negative number. Therefore, by adding these two numbers, you are essentially taking a difference.

Some investors consider this method to be crude and to lead to misleading free cash flow estimates because investing cash flows are not steady. In fact, they can be quite large one period (because a firm has made a major investment) and then practically non-existence the next. These investors feel it is much better to come up with an adjusted cash flow from investing number (which usually involves taking some kind of moving average).

Adjusting or normalizing cash flow from investing before using it to calculate free cash flow is not wrong. But this practice introduces an element of subjectivity into the results. This could be a good thing or bad thing depending upon the ability of the person doing the adjusting.