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Newell Rubbermaid: Why It'll Bounce Back

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Full Text (657 words)

How cold is Newell Rubbermaid? Let's just say Wall Street is so disgusted with the big housewares maker that in July, the last time CEO Joe Galli talked to analysts, he had to plead: "Maybe give us a little credibility." Sorry, Joe. The stock sank 17% that day and 10% more after Galli canceled an October meeting set to wow analysts with new products and the business outlook.

This is why the next time a pair of CEOs predict a merger of their companies will create synergies, you should tell them to stuff it in a 32-gallon Rubbermaid trash can. In the 10 years before the Rubbermaid deal, Newell's shareholders had grown used to annual average total returns of nearly 23% -- four percentage points ahead of the Standard & Poor's 500-stock index. In 1998, when Newell agreed to buy Rubbermaid with $5.8 billion worth of its stock, the two companies enjoyed a total stock market value of $12 billion. Today, at $22 a share, Newell Rubbermaid brings about half of that.

Investors can't hang this merger from hell on Galli; he came in as CEO from Amazon.com in 2001. And, even if Newell Rubbermaid has been guilty during his tenure of promising the Street too much, too fast -- in July, he lowered earnings guidance for 2003 -- the company is on a sounder footing than recent action in its stock implies. I can't give you odds on whether Galli will survive the current crisis -- and he isn't talking. But as I see it, if he does survive it'll be because the company shows solid progress and the stock recovers. If he doesn't, the stock will rally on hope of better management.

UNDERLYING THE TURMOIL is a steadily profitable, if slow-growing, maker of a gazillion everyday things: Rubbermaid containers, of course, plus Little Tikes toys, Sharpie, Parker, and Waterman pens, Calphalon cookware, and Levolor blinds. In the 12 months ended June, these products and more brought $262 million in net profit on revenue of $7.7 billion. Operating cash flow came to $711 million.

A nagging problem, however, is where all that cash flows next. Of the $711 million, $339 million went to capital projects. Of that, Rubbermaid consumed the greatest share among the company's four segments. Yet Rubbermaid in 2002 contributed just 35% of sales and even less of the company's operating profit (table). No one doubts that Newell wildly overpaid for Rubbermaid. The persistent question is whether it's continuing to overpay by plowing so much fresh cash back into Rubbermaid's new-product programs and productivity initiatives. Results in the first half ended June 30, when Rubbermaid sales grew just 1.4% and operating income actually fell 5%, suggest the answer is yes.

So why do I see opportunity in Newell Rubbermaid? Because whether it's Galli or another executive who does it, squeezing greater returns for shareholders out of a long-established company with familiar brands, strong operating cash flows, and a manageable balance sheet -- total debt is about half of capital -- is a far less daunting endeavor than, say, inventing and selling the next-generation cell phone. The dough, in other words, is already coming in the door, and investors now are getting annual dividends of 84 cents a share. That's a 3.8% yield on a $22 stock that trades for 0.8 times sales and 13 times the Street's most bearish estimate of next year's earnings. Get 'em while they're cold.

(available online)

Rubber Trouble

While Rubbermaid provides the largest share of its parent company's sales, its contribution to profits has been unimpressive.

	SEGMENT	% OF	OPERATING	% OF	CAPITAL	% OF
COMPANY	SALES	SALES	INCOME	O.I.	SPENDING	C.S.
Rubbermaid	2592	35	215	27	135	56
Sharpie	1909	26	323	41	41	17
Irwin	1727	23	136	17	46	19
Calphalon Home	1226	16	120	15	17	7

Dollar figures, in millions, are for 2002

Data: Company reports, BusinessWeek

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[Illustration]

Photo: Photograph: CASH STASH : Familiar brands -- and stroong cash flow -- can help the company survive the current crisis PHOTOGRAPH BY ROGER KENNY

Credit: Robert Barker