audit settlements, international restructuring initiatives and statutory rate changes. (Refer to Note 11 within Notes to Consolidated Financial Statements for further information.) For 2009, we expect our consolidated effective income tax rate to be approximately 30% to 31%. This could be impacted if pending uncertain tax matters, including tax positions that could be affected by planning initiatives, are resolved more or less favorably than we currently expect. Fluctuations in foreign currency exchange rates could also impact the effective tax rate as it is dependent upon the U.S. dollar earnings of foreign subsidiaries doing business in various countries with differing statutory tax rates.

Subsequent event

On January 14, 2009, we announced a precautionary hold on certain *Austin* and *Keebler* branded peanut butter sandwich crackers and certain *Famous Amos* and *Keebler* branded peanut butter cookies while the U.S. Food and Drug Administration and other authorities investigated Peanut Corporation of America ("PCA"), one of Kellogg's peanut paste suppliers for the cracker and cookie products. On January 16, 2009, Kellogg voluntarily recalled those products because the paste ingredients supplied to Kellogg had the potential to be contaminated with salmonella. The recall was expanded on January 31, February 2 and February 17, 2009 to include certain *Bear Naked*, *Kashi* and *Special K* products impacted by PCA ingredients.

We have incurred costs associated with the recalls and in accordance with U.S. GAAP we recorded certain items associated with this subsequent event in our fiscal year 2008 financial results.

The charges associated with the recalls reduced North America full-year 2008 operating profit by $34 million or $0.06 of EPS. We expect a similar impact in 2009. Of the total 2008 charges, $12 million related to estimated customer returns and consumer rebates and was recorded as a reduction to net sales; $21 million related to costs associated with returned product and the disposal and write-off of inventory which was recorded as cost of goods sold; and $1 million related to other costs which were recorded as SGA expense.

LIQUIDITY AND CAPITAL RESOURCES

Our principal source of liquidity is operating cash flows supplemented by borrowings for major acquisitions and other significant transactions. Our cash-generating capability is one of our fundamental strengths and provides us with substantial financial flexibility in meeting operating and investing needs.

Credit environment

The U.S. and global economies began a period of uncertainty starting in 2007. Financial markets continue to experience unprecedented volatility. Beginning in the third quarter of 2008 and thereafter, global capital and credit markets, including commercial paper markets, experienced increased instability and disruption.

Our Company's financial strength was evident throughout this period of uncertainty, as we continued to have access to the U.S. and Canadian commercial paper markets. Although interest rates on our U.S. commercial paper increased by an average of 200 basis points during the period from mid-September through October 2008, the average interest rate we paid for commercial paper borrowings in 2008 declined to 3.5% from an average of 5.4% in 2007. Our commercial paper and term debt credit ratings have not been affected by the changes in the credit environment, and the amount of our total debt outstanding remained relatively flat over the past three years.

If needed, we have additional sources of liquidity available to us. These sources include our access to public debt and/or equity markets, and the ability to sell trade receivables. Our Five-Year Credit Agreement, which expires in 2011, allows us to borrow up to $2.0 billion on a revolving credit basis. This source of liquidity is unused and available on an unsecured basis, although we do not currently plan to use it.

We monitor the financial strength of our third-party financial institutions, including those that hold our cash and cash equivalents as well as those who serve as counterparties to our credit facilities, our derivative financial instruments, and other arrangements.

We believe that our operating cash flows, together with our credit facilities and other available debt financing, will be adequate to meet our operating, investing and financing needs in the foreseeable future. However, there can be no assurance that continued or increased volatility and disruption in the global capital and credit markets will not impair our ability to access these markets on terms acceptable to us, or at all.

Operating activities

The principal source of our operating cash flow is net earnings, meaning cash receipts from the sale of our products, net of costs to manufacture and market our products. Our cash conversion cycle (defined as days of inventory and trade receivables outstanding less days of trade payables outstanding, based on a trailing 12 month average) is relatively short, equating to approximately 22 days for 2008, 24 days for 2007 and 26 days for 2006. The decrease in 2008 was the result of a decrease in days of inventory outstanding, while the decrease in 2007 reflected an increase in days of trade payables outstanding.

The following table presents the major components of our operating cash flow during the current and prior year-to-date periods:

(dollars in millions)	2008	2007	2006
Operating activities			
Net earnings	**$1,148**	$1,103	$1,004
year-over-year change	***4.1%***	*9.9%*	
Items in net earnings not requiring (providing) cash:			
Depreciation and amortization	**375**	372	353
Deferred income taxes	**157**	(69)	(44)
Other (a)	**119**	183	235
Net earnings after non-cash items	**1,799**	1,589	1,548
year-over-year change	***13.2%***	*2.6%*	
Pension and other postretirement benefit plan contributions	**(451)**	(96)	(99)
Changes in operating assets and liabilities:			
Core working capital (b)	**121**	16	(138)
Other working capital	**(202)**	(6)	99
Total	**(81)**	10	(39)
Net cash provided by operating activities	**$1,267**	$1,503	$1,410
year-over-year change	***−15.7%***	*6.6%*	

(a) Consists principally of non-cash expense accruals for employee compensation and benefit obligations.

(b) Inventory, trade receivables and trade payables.

Our net cash provided by operating activities for 2008 was $236 million lower than 2007, due primarily to a substantial increase in pension and other postretirement benefit plan contributions in 2008 and an unfavorable year-over-year variance in other working capital. Partially offsetting the decrease was the impact of changes in deferred income taxes and a favorable variance in core working capital.

Our net cash provided by operating activities for 2007 was $93 million higher than the comparable period of 2006, due primarily to growth in cash-basis earnings and favorable total working capital performance. As compared to 2006, the favorable movement in core working capital during 2007 was related principally to higher accounts payable, which were due in part to increased payment terms in international locations.

In 2008, core working capital was an average of 6.2% of net sales, an improvement of 0.6% compared with 2007. In 2007, core working capital was an average of 6.8% of net sales, consistent with 2006. We manage core working capital through timely collection of accounts receivable, extending terms on accounts payable and careful monitoring of inventory.

Other working capital in 2008 reflected an increase in cash paid associated with hedging programs, cash paid for advertising and promotion, and the impact of changes in accrued salaries and wages. Other working capital in 2007 was a use of cash versus a source of cash in 2006. The difference related to a year-over-year increase in the amount of income tax payments.

Recent adverse conditions in the equity markets caused the actual rate of return on our pension and postretirement plan assets to be significantly below our assumed long-term rate of return of 8.9%. As a result, we decided to make additional contributions to our pension and postretirement plans amounting to $400 million in the fourth quarter of 2008. Our total pension and postretirement plan funding for 2008 totaled $451 million, while funding in 2007 and 2006 amounted to $96 million and $99 million, respectively.

In 2006, the Pension Protection Act (PPA) became law in the United States. The PPA revised the basis and methodology for determining defined benefit plan minimum funding requirements as well as maximum contributions to and benefits paid from tax-qualified plans. The PPA will ultimately require us to make additional contributions to our U.S. plans. We believe that we will not be required to make any contributions under PPA requirements until 2011. Our projections concerning timing of PPA funding requirements are subject to change primarily based on general market conditions affecting trust asset performance and our future decisions regarding certain elective provisions of the PPA.

We currently project that we will make total U.S. and foreign plan contributions in 2009 of approximately $100 million. Actual 2009 contributions could be different from our current projections, as influenced by our decision to undertake discretionary funding of our benefit trusts versus other competing investment priorities, future changes in government requirements, trust asset performance, renewals of union contracts, or higher-than-expected health care claims cost experience.

Our management measure of cash flow is defined as net cash provided by operating activities reduced by expenditures for property additions. We use this non-GAAP financial measure of cash flow to focus management and investors on the amount of cash available for debt repayment, dividend distributions, acquisition opportunities, and share repurchases. Our cash flow metric is reconciled to the most comparable GAAP measure, as follows:

(dollars in millions)	2008	2007	2006
Net cash provided by operating activities	**$1,267**	$1,503	$1,410
Additions to properties	**(461)**	(472)	(453)
Cash flow	**$806**	$1,031	$957
year-over-year change	***−21.8%***	*7.7%*	

Our 2008 cash flow (as defined) reflects the impact of the additional pension contributions we made in the fourth quarter of 2008. For 2009, we are expecting cash flow (as defined) in the range of $1,050 million to $1,150 million. This projection assumes an adverse impact on 2009 cash flow of approximately $100 million associated with changes in foreign currency exchange rates. We expect to achieve our target principally through operating profit growth, lower contributions to pension and other postretirement benefit plans in 2009, and continued prudent management of our working capital.

Investing activities

Our net cash used in investing activities for 2008 amounted to $681 million, an increase of $80 million compared with 2007. Net cash used in investing activities of $601 million in 2007 increased by $156 million compared with 2006.

Cash paid for acquisitions during 2008 and 2007 were the primary drivers of increases in cash used in investing activities, as we expanded our platform for future growth with acquisitions in Russia, China, the U.S. and Australia. Acquisitions are discussed in Note 2 within Notes to Consolidated Financial Statements.

Cash paid for additions to properties as a percentage of net sales amounted to 3.6% in 2008, 4.0% in 2007 and 4.2% in 2006. In 2008, capital spending consisted primarily of construction costs to increase capacity in Europe and to expand our global research center in Battle Creek, Michigan. In 2007, we made capacity expansions to accommodate sales growth, including the purchase of a previously leased snacks manufacturing facility in Chicago, Illinois.

We expect our K LEAN manufacturing efficiency initiative to result in a trend toward lower capital spending. Going forward, our long-term target for capital spending is between 3.0% and 4.0% of net sales.

Our 2009 capital plan includes spending for a new facility to manufacture ready-to-eat cereal in Mexico and continued spending on the ongoing project to expand the global research center in Battle Creek, Michigan. The expansion of the W. K. Kellogg Institute for Food and Nutrition Research reflects our commitment to research and innovation which is a key driver to the growth of our business.

Financing activities

Our net cash used in financing activities for 2008, 2007 and 2006 amounted to $780 million, $788 million and $789 million, respectively.

In March 2008, we issued $750 million of five-year 4.25% fixed rate U.S. Dollar Notes under an existing shelf registration statement. We used proceeds of $746 million from issuance of this long-term debt to retire a portion of our commercial paper. In conjunction with this debt issuance, we entered into interest rate swaps with notional amounts totaling $750 million, which effectively converted this debt from a fixed rate to a floating rate obligation for the duration of the five-year term. In 2008, we had cash outflows of $465 million in connection with the repayment of five-year U.S. Dollar Notes at maturity in June 2008. That debt had an effective interest rate of 3.35%.

In January 2007, we increased our available credit via a $400 million unsecured 364-Day Credit Agreement. The $400 million Credit Agreement expired in January 2008 and we decided not to renew it. In February 2007, we redeemed Euro Notes for $728 million. To partially finance this redemption, we established a program to issue euro commercial paper notes up to a maximum aggregate amount outstanding at any time of $750 million or its equivalent in alternative currencies. In December 2007, the Company issued $750 million of five-year 5.125% fixed rate U.S. Dollar Notes under the existing shelf registration statement, using the proceeds to replace a portion of our U.S. commercial paper.

During 2008, 2007 and 2006, we repurchased $650 million of our common stock each year under programs authorized by our Board of Directors. The number of shares repurchased amounted to approximately 13 million, 12 million and 15 million shares, respectively, in 2008, 2007 and 2006. The 2006 activity consisted principally of a private transaction with the W. K. Kellogg Foundation Trust to repurchase approximately 13 million shares for $550 million. On February 4, 2009, the Board of Directors authorized a $650 million share repurchase authorization for 2009 that we plan to execute largely in the second half of the year. The Board also canceled a $500 million share repurchase authorization that it had authorized in third quarter 2008. We made no purchases under the $500 million share repurchase authorization because of our decision to use cash to fund pension plans and reduce commercial paper in the fourth quarter of 2008.

We paid quarterly dividends to shareholders totaling $1.30 per share in 2008, $1.202 per share in 2007 and $1.137 per share in 2006. Cash paid for dividends increased by 8.2% in 2008, and by 5.7% in 2007. Our objective is to maintain our dividend pay-out ratio between 40% and 50% of reported net earnings.

At January 3, 2009, our total debt was $5.5 billion, approximately level with the balance at year-end 2007. Our long-term debt agreements contain customary covenants that limit the Company and some of its subsidiaries from incurring certain liens or from entering into certain sale and lease-back transactions. Some agreements also contain change in control provisions. However, they do not contain acceleration of maturity clauses that are dependent on credit ratings. A change in the Company's credit ratings could limit our access to the U.S. short-term debt market and/or increase the cost of refinancing long-term debt in the future. However, even under these circumstances, we would continue to have access to our aforementioned credit facilities.

We continue to believe that we will be able to meet our interest and principal repayment obligations and maintain our debt covenants for the foreseeable future, while still meeting our operational needs, including the pursuit of selected bolt-on acquisitions. This will be accomplished through our strong cash flow, our short-term borrowings, and our maintenance of credit facilities on a global basis.