General Electric (GE)

Updated May 25th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	$14	**5 Year CAGR Estimate:**	11.9%	**Quality Percentile:**	N/A
Fair Value Price:	$17	**5 Year Growth Estimate:**	5.0%	**Momentum Percentile:**	N/A
% Fair Value:	84%	**5 Year Valuation Multiple Estimate:**	3.5%	**Total Return Percentile:**	N/A
Dividend Yield:	3.4%	**5 Year Price Target**	$21	**Valuation Percentile:**	N/A

Overview & Current Events

General Electric is a diversified digital industrial company that was established 125 years ago and has a market cap of $123 B. General Electric's long history and large market cap make it one of the most well-known dividend stocks around.

General Electric has dramatically underperformed the market in the last 12 months, declining 49% versus a 13% gain for the S&P 500. There are multiple reasons for the decline. First, the company lowered its results for the last two years in retrospect due to accounting issues. In addition, its power segment has been struggling due to lower demand, which has been driven by energy efficiency and the growth of renewable sources, coupled with price pressure due to market overcapacity. Moreover, its net debt (total liabilities – cash – receivables) has become excessive, as it currently stands at $207.3 B. Furthermore, the company has posted poor free cash flows in the last two years and was thus forced to cut its dividend by 50% a few months ago.

On the other hand, the company is currently in turnaround mode, trying to improve its performance on many fronts. It cut its structural costs by $1.7 B last year and expects to cut another $2 B this year. In addition, it expects to divest $5 B to $10 B of non-core assets this year in order to reduce its debt load. Moreover, its aviation and healthcare segments are growing at a fast pace, with 26% and 11% growth in operating profit in Q1, respectively. Overall, the company is going through a major transformation. It is trying to divest several assets in order to reduce its debt load, simplify its portfolio, and focus on its more promising segments.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.78	$1.03	$1.15	$1.31	$1.52	$1.64	$1.65	$1.32	$1.49	$1.05	***$1.00***	***$1.28***
DPS	$1.24	$0.61	$0.46	$0.61	$0.70	$0.79	$0.89	$0.92	$0.92	$0.84	***$0.48***	***$0.64***

Analysts expect EPS of $0.97 while GE management expects EPS between $1.00 and $1.07 this year. Therefore, it is reasonable to expect EPS around $1.00 this year.

While General Electric has exhibited poor performance in the last two years, its base has become low and hence the company can start growing off a low base in the upcoming years. Its challenged power segment contributes only 9% of its total operating income whereas the thriving segments of aviation and healthcare contribute 78% of total operating income. The aviation and healthcare segments grew their operating income by 9% last year and by 26% and 11%, respectively, in Q1. Thanks to these parts of its business, General Electric can grow its EPS by at least 5.0% in the upcoming years, from $1.00 this year to $1.28 in 2023. The industrial titan may grow even faster but it is prudent to be conservative due to the uncertainty that always surrounds turnaround cases.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	15.7	13.0	14.4	13.9	13.3	14.7	15.7	20.3	20.4	24.8	***14.0***	***16.6***
Avg. Yld.	4.4%	4.6%	2.8%	3.4%	3.5%	3.3%	3.4%	3.4%	3.0%	3.2%	***3.4%***	***3.0%***

Due to its poor performance, General Electric is currently trading around 9-year lows. Consequently, its current P/E of 14.0 is lower than its 10-year average P/E of 16.6. The low P/E seems to be justified now that the company is going through a major transformation and the success of its turnaround is unknown. However, as the uncertainty subsides in the upcoming years, the stock is likely to revert towards its average valuation level. If the stock returns to its average P/E ratio within the next five years, it will enjoy a 3.5% annualized gain thanks to the expansion of its P/E ratio.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	12.3%	10.1%	10.3%	10.9%	10.6%	5.1%	5.1%	7.0%	9.9%	8.0%	***8.0%***	***9.0%***
Debt/A	85.8%	84.0%	83.4%	83.6%	81.2%	79.2%	79.1%	79.1%	78.0%	77.4%	***80.0%***	***80.0%***
Int. Cov.	1.8	1.5	1.9	2.4	2.4	4.2	4.8	3.4	2.8	0.8	***2.0***	***2.5***
Payout	69.7%	59.2%	40.0%	46.6%	46.1%	48.2%	53.9%	69.7%	61.7%	80.0%	***48.0%***	***50.0%***
Std. Dev.	35.3%	63.8%	30.0%	29.2%	17.2%	15.4%	13.9%	21.6%	16.7%	19.4%	***18.0%***	***17.0%***

General Electric has cut its dividend twice in the last decade. Moreover, as the company is divesting several assets and is using the proceeds to reduce its debt load, some analysts claim that the company is reducing its capacity to generate free cash flows. As a result, these analysts expect another dividend cut in the near future. However, General Electric is divesting low-return assets. In addition, it currently has a healthy payout ratio of 48.0%. Therefore, it is not likely to cut its dividend again anytime soon. The company has an excessive debt load. Improvement on that front will do much to de-risk General Electric's operations ahead.

Final Thoughts & Recommendation

General Electric has struggled over the last several years. It has dramatically underperformed the S&P, cut its dividend for a second time in the last decade, and is now trading around 9-year lows. Therefore, it is only natural that General Electric stock is out of favor among most investors.

However, the company seems to be at an inflection point. It is becoming leaner, more efficient, and is focusing on its most promising segments. Those who have the courage to buy shares during such times are usually rewarded with excellent long-term returns. Even if General Electric grows its EPS by just 5.0% per year in the next five years, it is likely to reward investors with an 11.9% average annual return thanks to its 3.4% dividend and a 3.5% annualized gain thanks to P/E expansion. Nevertheless, due to its short-term negative momentum, the stock is suitable only for the investors who can maintain a long-term perspective and tolerate higher levels of risk and uncertainty.

Total Return Breakdown by Year