General Electric (GE)

Updated July 20th, 2018 by Ben Reynolds

Key Metrics

Current Price:	$13	**5 Year CAGR Estimate:**	13.5%	**Volatility Percentile:**	66.4%
Fair Value Price:	$17	**5 Year Growth Estimate:**	5.0%	**Momentum Percentile:**	1.4%
% Fair Value:	79%	**5 Year Valuation Multiple Estimate:**	4.8%	**Valuation Percentile:**	87.7%
Dividend Yield:	3.7%	**5 Year Price Target**	$21	**Total Return Percentile:**	82.1%

Overview & Current Events

General Electric (GE) is a large diversified manufacturer that was established 125 years ago. Today, GE has both a market capitalization and annual revenues of ~$120 billion.

GE had 2 major announcements since our last report on the company. On June 26th, the company announced a new strategic plan for growth and shareholder value creation. The company plans to focus on its Aviation, Power, and Renewable Energy segments. These 3 segments accounted for 62% of GE's profit (before GE Capital losses) over the last 6 months, for comparison. The company announced it will liquidate ~20% of its Healthcare segment, and spin-off the remaining 80% to shareholders in the next 12 to 18 months. The Healthcare segment is the company's second largest by profit (behind only Aviation), responsible for 26% of profit for GE over the last 6 months. Additionally, GE will dispose of its 62.5% ownership in Baker Hughes GE (BHGE), which is worth $22 billion at current prices. The company plans to deleverage and achieve a net debt-to-EBITDA ratio (excluding GE Capital) of 2.5 by 2020. Additionally, Larry Culp will succeed Jack Brennan as lead director of GE. On a positive note for dividend investors, the company plans to maintain its current $0.12 per quarter dividend through the above restructuring.

GE also recently released (7/20/18) its 2nd quarter 2018 results. Industrial revenue and adjusted earnings-per-share (EPS) declined 3% and 10% respectively versus the same quarter a year ago. The company is making progress through cutting costs, but adjusted earnings-per-share continue to fall. Shares have declined nearly 50% over the last 12 months as GE continues to struggle.

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***

GE's management expects adjusted earnings of $1.00 to $1.07 for fiscal 2018. We are setting our expectations low, at the bottom of this range, due to GE's weak performance over the last decade.

GE's growth history leaves much to be desired. Expected EPS for fiscal 2018 *are lower than during the worst of the Great Recession* (2009). Additionally, GE's dividend is at less than half of 2008 levels. General Electric's plan to spin-off portions of its business, pay down debt, and continue to sharpen its focus are positives. We expect the company to return to modest growth of around 5% annually over the next 5 years, barring a major economic downturn.

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	***13.1***	***16.6***
Avg. Yld.	4.4%	4.6%	2.8%	3.4%	3.5%	3.3%	3.4%	3.4%	3.0%	3.2%	***3.7%***	***3.0%***

GE stock is currently trading around 2009 level prices. The company currently has a P/E ratio of just 13.1 using expected 2018 adjusted EPS. GE is undervalued relative to its historical average price-to-earnings ratio of 16.6. We expect GE's price-to-earnings ratio to mean revert over the next 5 years as the company deleverages and returns to modest growth.

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. The company's management plans to sustain the current $0.48 annual dividend throughout the continuing restructuring, and presumably beyond. With a payout ratio of just 48%, GE's dividend is unlikely to be cut again soon. The company's interest coverage ratio is especially worrisome. Make no mistake, GE has elevated risk thanks to its high debt levels. The company plans to reduce its interest coverage ratio to more reasonable levels over the next several years.

Final Thoughts & Recommendation

General Electric *used to be* an iconic blue-chip stock. With two dividend cuts in the last decade and high leverage, the company is far from a safe dividend growth stock today. Investors looking for a stable, 'sleep well at night' stock should avoid General Electric. If the global economy were to see another severe recession, General Electric would likely be unable to service its debt.

With that said, there are positives to a GE investment at current prices. The company is clearly undervalued relative to its historical average. The low valuation has in turn given GE strong expected total returns of 13.5% a year. The company's management is divesting assets and using the proceeds to put GE back on solid footing. There's certainly potential upside here. Still, it's difficult to recommend this stock in clear conscience with its high debt levels and spotty recent history. Only the most risk-tolerant investors should consider investing in GE. Even then, this stock should not be a core position in anyone's portfolio due to its elevated risk.

Total Return Breakdown by Year