General Electric (GE)

Updated April 30th, 2019 by Eli Inkrot

Key Metrics

Current Price:	$10	**5 Year CAGR Estimate:**	4.0%	**Volatility Percentile:**	87.6%
Fair Value Price:	$6	**5 Year Growth Estimate:**	14.9%	**Momentum Percentile:**	7.1%
% Fair Value:	182%	**5 Year Valuation Multiple Estimate:**	-11.3%	**Growth Percentile:**	97.9%
Dividend Yield:	0.4%	**5 Year Price Target**	$11	**Valuation Percentile:**	2.8%
Dividend Risk Score:	C	**Retirement Suitability Score:**	F	**Total Return Percentile:**	23.9%

Overview & Current Events

Tracing its roots back to Thomas Edison in the 1870's, General Electric is a $87 billion diversified manufacturer headquartered in Boston, MA. The company operates in eight segments: Power, Renewable Energy, Aviation, Oil & Gas, Healthcare, Transportation, Lighting and GE Capital. However, the company is undergoing a major turnaround. On June 26th, 2018 the company announced a new strategic plan, to focus on its Aviation, Power, and Renewable Energy segments. The company announced it will monetize ~20% of its Healthcare segment, and spin-off the remaining 80% to shareholders in the next 12 to 18 months. Additionally, GE will dispose of its ownership in Baker Hughes GE (BHGE). The company plans to deleverage and achieve a net debt-to-EBITDA ratio (excluding GE Capital) of 2.5x by 2020.

On April 30th, 2019 General Electric released Q1 2019 results for the period ending March 31st, 2019. For the quarter revenue came in at $27.3 billion, representing a 2% decline compare to Q1 2018, as 12% and 4% respective gains in Aviation and Oil & Gas were more than offset by a 22% decline in the Power segment. Adjusted earnings-per-share came in at $0.14 compared to $0.15 in the year ago period.

Previously, General Electric had taken a variety of actions to de-leverage its balance sheet including reducing the quarterly dividend, accelerating the sell down of Baker Hughes and selling industrial and capital assets. The company continued this path in Q1 2019, with the sale of BioPharma to Danaher for $20 billion in cash proceeds and closing the merger with Wabtec, which resulted in $2.9 billion in cash proceeds and a 24.9% ownership stake in Wabtec. General Electric also said it expects adjusted earnings-per-share to be in the $0.50 to $0.60 range this year.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$1.03	$1.15	$1.31	$1.52	$1.64	$1.65	$1.32	$1.49	$1.05	$0.65	***$0.55***	***$1.10***
DPS	$0.61	$0.46	$0.61	$0.70	$0.79	$0.89	$0.92	$0.92	$0.84	$0.48	***$0.04***	***$0.04***
Shares	10,663	10,615	10573	10,406	10,061	10,057	9,373	8,742	8,680	8,702	***8,700***	***8,700***

GE's growth history leaves much to be desired. Earnings for 2018 came in much lower than the company's performance during the last recession. General Electric's plan to spin-off portions of its business, pay down debt, and continue to sharpen its focus are generally positive as the company is recognizing that it is too leveraged and is taking direct actions to reduce its debt. However, we are cautious in that it is difficult to cut your way to growth. This is especially true when you're thinking about getting rid of some of the crown jewels, in this case the Healthcare segment.

GE faces continued challenges in the power business, too much debt, and ongoing liabilities in the GE Capital segment. All of these areas are being addressed, but will require patience. While some growth is expected, this is basically just getting back to average operating results after stumbling in the last few years. Our above average expected growth rate near 15% is offset by the dip in earnings in 2018 and 2019, and balances out with the valuation headwind.

Don't be fooled by GE's claim of having paid a dividend for more than 100 years. The company has cut its dividend three times in the last decade - in 2009, 2017 and now 2019. The company's current dividend is a negligible $0.01 per quarter. While the company has stated that it anticipates a dividend payout ratio that is in-line with peers over time, we believe it is prudent to keep the payout low and continue shoring up the balance sheet.

Disclosure: This analyst is long the security discussed in this research report.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	13.0	14.4	13.9	13.3	14.7	15.7	20.3	20.4	24.8	19.8	***18.2***	***10.0***
Avg. Yld.	4.6%	2.8%	3.4%	3.5%	3.3%	3.4%	3.4%	3.0%	3.2%	2.9%	***0.4%***	***0.4%***

The last time shares traded around $10 per share was back in 2009 during the financial crisis. The only difference today is that expected earnings are lower than they were back then. GE's average P/E ratio over the last decade has been about 17 times earnings. However, we believe a much lower multiple is warranted considering the difficulties the firm has been and will continue to face, along with the uncertain growth prospects from this point. The current valuation implies a significant valuation headwind; however, this is largely a result of currently depressed earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	59%	40%	47%	46%	48%	54%	70%	62%	80%	74%	***7%***	***4%***

GE has competitive advantages in its Aviation and Healthcare segments, as it offers a best-in-breed product that tends to create sticky customer relationships. However, the problem is that the other segments do not enjoy the same type of advantages and indeed have even been a drag on the business.

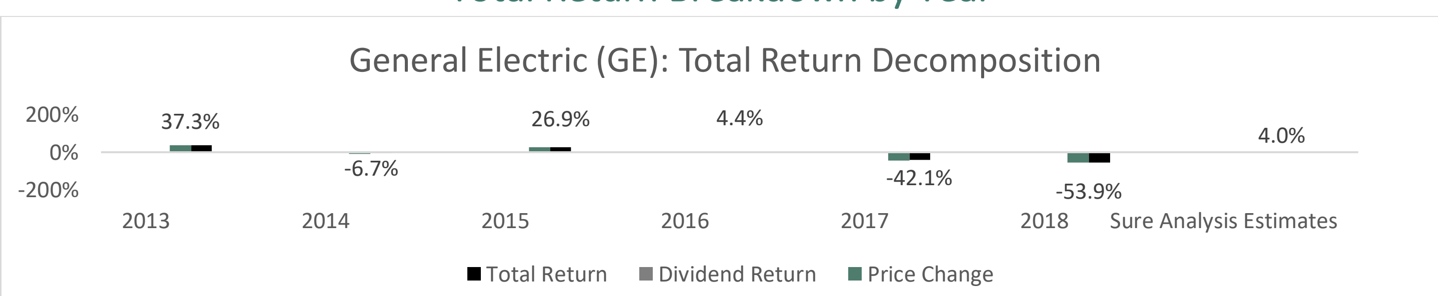
During the last recession GE posted earnings-per-share of $2.20, $1.78, $1.03 and $1.15 during the 2007 through 2010 stretch and cut its dividend. Then, it faltered again seeing earnings of $1.65 in 2014 erode to $0.65 in 2018 and again cutting its dividend, twice more. This is not just a cautionary tale but an example to remember – even the seemingly best businesses in the world can falter as past mistakes and a high debt load caught up to the company.

Still, there are positives. The dividend cuts are not welcome by income investors, but they do make it easier to refocus the company's profits on fixing the business. Moreover, we are encouraged by GE's acknowledgement and plans to attack the debt load at every angle. Still, time will tell whether or not adequate progress is being made.

Final Thoughts & Recommendation

Shares are more or less unchanged since our last update. GE has gone from being a sure storied business, admired for its industrial conglomerate might, to hoping to be a turn-around story stock. While there are some bright spots in the business, there are too many unknowns for us to be encouraged. Keep in mind that the 4% total annual return expectation appears somewhat reasonable to us, but it is based on an artificially high expected growth rate being netted out against a significant valuation drag, as a result of recently depressed earnings. Should GE regain its footing, shares will be attractive from this point as the "snap back" effect as it relates to growth, valuation and the dividend would be significant, especially with a greatly depressed share price. However, that is a speculation that we are not yet comfortable making. Overall, we rate the company a sell at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue ($B)	155.28	148.42	141.48	144.12	110.14	116.41	115.16	119.69	120.47	121.62
Gross Profit	79357	62193	59441	58215	28275	31064	30164	28414	25389	23885
Gross Margin	51.1%	41.9%	42.0%	40.4%	25.7%	26.7%	26.2%	23.7%	21.1%	19.6%
SG&A Exp.	40426	38033	36841	35897	18773	17963	20439	19359	21912	18575
D&A Exp.	10619	9786	8986	9192	5202	4953	4847	4997	5139	N/A
Operating Profit	28304	18226	23733	21049	12609	13879	11952	13060	5102	5310
Op. Margin	18.2%	12.3%	16.8%	14.6%	11.4%	11.9%	10.4%	10.9%	4.2%	4.4%
Net Profit	11025	11644	14151	13641	13057	15233	-6126	8831	-5786	-22B
Net Margin	7.1%	7.8%	10.0%	9.5%	11.9%	13.1%	-5.3%	7.4%	-4.8%	-18.4%
Free Cash Flow	15783	26324	20722	16212	21756	20575	11804	-8192	2506	N/A
Income Tax	-1148	1039	5745	2534	1219	773	6485	-464	-3043	583

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets ($B)	781.90	747.79	718.19	685.00	656.56	654.95	493.07	365.18	377.95	309.10
Cash & Equivalents	70488	78943	84501	77268	88555	70025	70483	48129	43299	N/A
Acc. Rec. ($B)	16.46	321.63	300.40	277.14	263.33	36.68	39.08	36.32	34.77	27.60
Inventories	11987	11526	13792	15374	17325	17689	22515	22354	21923	19300
Goodwill/Int. ($B)	76.83	74.36	84.69	85.09	91.96	66.39	83.33	86.88	104.24	77.80
Total Liab. ($B)	656.77	623.60	600.06	556.53	519.78	518.12	392.93	287.69	295.96	257.60
Accounts Payable	19527	14656	16400	15654	16471	12067	13680	14435	15153	N/A
LT Debt ($B)	469.9	478.6	453.4	413.8	383.0	261.4	197.6	136.2	134.6	110.0
Total Equity ($B)	117.3	118.9	116.4	123.0	130.6	128.2	98.3	75.8	64.3	31.0
D/E Ratio	4.01	4.02	3.89	3.36	2.93	2.04	2.01	1.80	2.09	3.55

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	1.4%	1.5%	1.9%	1.9%	1.9%	2.3%	-1.1%	2.1%	-1.6%	-6.5%
Return on Equity	9.9%	9.9%	12.0%	11.4%	10.3%	11.8%	-5.4%	10.1%	-8.3%	-46.9%
ROIC	1.8%	1.9%	2.4%	2.4%	2.5%	3.3%	-1.8%	3.5%	-2.7%	-11.8%
Shares Out.	10,663	10,615	10573	10,406	10,061	10,057	9,373	8,742	8,680	8,700
Revenue/Share	14.63	13.90	13.32	13.64	10.70	11.50	11.50	13.11	13.87	13.99
FCF/Share	1.49	2.47	1.95	1.53	2.11	2.03	1.18	-0.90	0.29	N/A

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.