General Electric (GE)

Updated October 28th, 2020 by Eli Inkrot

Key Metrics

Current Price:	$7.40	**5 Year CAGR Estimate:**	4.1%	**Market Cap:**	$65 B
Fair Value Price:	$5.50	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date[1]:**	12/20/20
% Fair Value:	135%	**5 Year Valuation Multiple Estimate:**	-5.8%	**Dividend Payment Date[1]:**	01/27/21
Dividend Yield:	0.5%	**5 Year Price Target**	$9.00	**Years Of Dividend Growth:**	0
Dividend Risk Score:	F	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	N/A

Overview & Current Events

Tracing its roots back to Thomas Edison in the 1870's, General Electric is a $65 billion diversified manufacturer headquartered in Boston, MA. The company previously operated eight segments: Power, Renewable Energy, Aviation, Oil & Gas, Healthcare, Transportation, Lighting and GE Capital. However, the company is undergoing a major transformation. General Electric has taken a variety of actions to de-leverage its balance sheet including reducing the quarterly dividend, accelerating the sell down of Baker Hughes (to be fully monetized in three years) and selling industrial and capital assets. The company continued this path in Q1 2019 with the sale of BioPharma to Danaher and closing the GE Transportation merger and spin-off with Wabtec, with GE's portion eventually divested by Q3 2019.

On October 28th, 2020 General Electric released Q3 2020 results for the period ending September 30th, 2020. For the quarter revenue came in at $19.42 billion, representing a 16.9% decline compared to Q3 2019. Small gains in Power (up 2.5%) and Renewable Energy (up 2.3%) were more than offset by substantial declines in Aviation (down -39.3%) and Healthcare (down -7.3%). Reported earnings-per-share equaled -$0.14 compared to -$1.08 prior. On an adjusted basis, earnings-per-share equaled $0.06 versus $0.15 in the year ago quarter.

Prior to the pandemic, General Electric provided a 2020 outlook, expecting adjusted earnings-per-share to be in the $0.50 to $0.60 range. However, this guidance has since been withdrawn and results are likely to be much lower.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$1.15	$1.31	$1.52	$1.64	$1.65	$1.32	$1.49	$1.05	$0.65	$0.65	***$0.05***	***$0.81***
DPS	$0.46	$0.61	$0.70	$0.79	$0.89	$0.92	$0.92	$0.84	$0.48	$0.04	***$0.04***	***$0.04***
Shares[2]	10,615	10573	10,406	10,061	10,057	9,373	8,742	8,680	8,702	8,724	***8,760***	***8,760***

GE's growth history leaves much to be desired. Earnings for 2018 and 2019 came in much lower than the company's performance during the last recession. General Electric's plan to transform 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.

GE faces continued challenges in the power business, too much debt, and ongoing liabilities in the GE Capital segment. And this was before the COVID-19 pandemic. We expect General Electric to post materially lower earnings this year, which could be too optimistic if the crisis lasts longer than anticipated. For the purposes of valuation and calculating a fair value estimate, we are using $0.50 in underlying earnings power – in-line with the lower end of the company's guidance prior to the crisis taking hold. Potential growth of 10% appears outsized, due to coming off a reduced base.

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 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 forecast allow payout while the company continues shoring up its balance sheet.

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[1] Estimate

[2] In millions.

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

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	14.4	13.9	13.3	14.7	15.7	20.3	20.4	24.8	19.8	15.2	***14.8***	***11.0***
Avg. Yld.	2.8%	3.4%	3.5%	3.3%	3.4%	3.4%	3.0%	3.2%	2.9%	0.4%	***0.5%***	***0.5%***

General Electric's average P/E ratio over the last decade has been about 17 times earnings. However, we believe a much lower multiple of 11 times earnings is warranted considering the difficulties the firm has and will continue to face, along with the uncertain growth prospects from this point. Even with shares down materially, the current valuation implies the potential for a valuation headwind moving forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	40%	47%	46%	48%	54%	70%	62%	80%	74%	6%	***8%***	***5%***

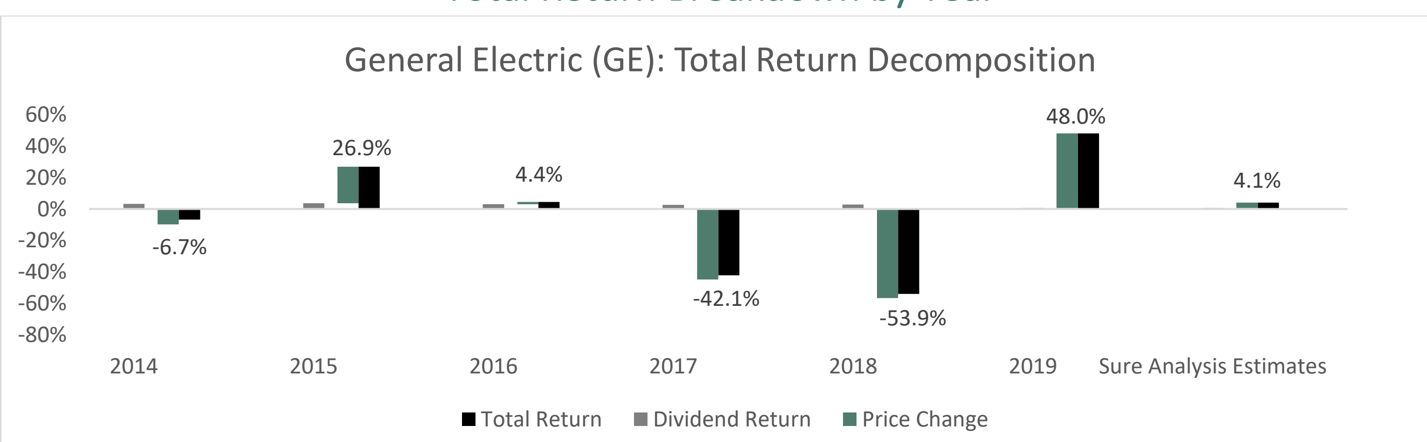
GE has competitive advantages in its Aviation and Healthcare segments, as it offers a best-in-breed product that tends to create sticky customer relationships. However, the problem is that the other segments do not enjoy the same type of advantages and indeed have even been a drag on the business. Moreover, Aviation in particular will be tested during the ongoing COVID-19 pandemic and its aftermath. During the last recession GE posted earnings-per-share of $2.20, $1.78, $1.03 and $1.15 for 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.

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 up 12% since our last update. GE has gone from being a storied business, admired for its industrial conglomerate might, to hoping to be a turn-around story stock. While there are some bright spots, there are too many unknowns especially amid the current crisis. Total return potential comes in at 4.1% per annum, stemming from 10% growth to get back to "normalized" profit and a 0.5% dividend, offset by a valuation headwind. Should GE regain its footing, shares could be attractive from this point as the "snap back" effect related to growth, valuation and the dividend would be significant. However, that is speculation, and we continue rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue ($B)	148.4	141.5	144.1	110.14	116.4	115.2	119.69	120.5	121.6	95215
Gross Profit	62193	59441	58215	28275	31064	30164	28414	25389	23885	22655
Gross Margin	41.9%	42.0%	40.4%	25.7%	26.7%	26.2%	23.7%	21.1%	19.6%	23.8%
SG&A Exp.	38033	36841	35897	18773	17963	20439	19359	21912	18575	17243
D&A Exp.	9786	8986	9192	5202	4953	4847	4997	5139	N/A	5595
Operating Profit	18226	23733	21049	12609	13879	11952	13060	5102	5310	5412
Op. Margin	12.3%	16.8%	14.6%	11.4%	11.9%	10.4%	10.9%	4.2%	4.4%	5.7%
Net Profit	11644	14151	13641	13057	15233	-6126	8831	-5786	-22B	-4979
Net Margin	7.8%	10.0%	9.5%	11.9%	13.1%	-5.3%	7.4%	-4.8%	-18%	-5.2%
Free Cash Flow	26324	20722	16212	21756	20575	11804	-8192	2506	N/A	2677
Income Tax	1039	5745	2534	1219	773	6485	-464	-3043	583	726

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets ($B)	747.79	718.19	685.00	656.56	654.95	493.07	365.18	377.95	309.10	266.05
Cash & Equivalents	78943	84501	77268	88555	70025	70483	48129	43299	N/A	36394
Acc. Rec. ($B)	321.63	300.40	277.14	263.33	36.68	39.08	36.32	34.77	27.60	15.73
Inventories	11526	13792	15374	17325	17689	22515	22354	21923	19300	14104
Goodwill/Int. ($B)	74.36	84.69	85.09	91.96	66.39	83.33	86.88	104.24	77.80	37.39
Total Liab. ($B)	623.60	600.06	556.53	519.78	518.12	392.93	287.69	295.96	257.60	236.19
Accounts Payable	14656	16400	15654	16471	12067	13680	14435	15153	N/A	15926
LT Debt ($B)	478.6	453.4	413.8	383.0	261.4	197.6	136.2	134.6	110.0	90.9
Total Equity ($B)	118.9	116.4	123.0	130.6	128.2	98.3	75.8	64.3	31.0	28.3
D/E Ratio	4.02	3.89	3.36	2.93	2.04	2.01	1.80	2.09	3.55	3.21

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	1.5%	1.9%	1.9%	1.9%	2.3%	-1.1%	2.1%	-1.6%	-6.5%	-1.7%
Return on Equity	9.9%	12.0%	11.4%	10.3%	11.8%	-5.4%	10.1%	-8.3%	-46.9%	-16.8%
ROIC	1.9%	2.4%	2.4%	2.5%	3.3%	-1.8%	3.5%	-2.7%	-11.8%	-3.6%
Shares Out.	10,615	10573	10,406	10,061	10,057	9,373	8,742	8,680	8,702	8,724
Revenue/Share	13.90	13.32	13.64	10.70	11.50	11.50	13.11	13.87	13.99	10.91
FCF/Share	2.47	1.95	1.53	2.11	2.03	1.18	-0.90	0.29	N/A	0.31

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