General Electric

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Julian Mitchell: I think we're ready to get underway. It's my pleasure to have here Larry Culp, Chairman and Chief Executive of GE. As a reminder, for that QR code, please take the time to scan it, send me any questions, and also complete the audience response survey questions and we'll disseminate the results of those in due course. Getting to it, Larry, thank you so much for being here. Maybe open up with any initial remarks before Q&A.

Larry Culp: Sure. Sure, Julian, thank you, and thanks for having us. A lot happening at GE. Appreciate everybody's interest in what we're up to at the company. You probably saw just a couple of weeks ago, we put out our annual report and our 10-K, really the best way to cap what was in many respects a historic year for us at GE. Really pleased with the progress in so many ways. Financially, it was a strong bottom line year from an earnings', from an op margin perspective, and certainly from a cash flow view. But I think beyond the numbers, what we were able to do strategically with the GECAS/AerCap merger, and in turn the consolidation of GE Capital, in turn what that allowed us to do with respect to de-leveraging, now in excess of $87 billion of debt retired, that doesn't happen overnight. A lot of good work in that regard. We'll continue to reshape the portfolio. You saw the announcement with respect to our steam nuclear business just a couple of weeks ago. Putting that with our French customer EDF, a better home for that business frankly, gives us an opportunity to focus in some other areas. So that strategic reshaping will continue.

But I also think when you look at what we're doing operationally, that's really what undergirds not only the financial performance but I think the trajectory for the company going forward. We talk a lot about Lean, that's a critical part of the transformation of the company. In addition to just running in a more decentralized manner. We report in 4 segments, but it's really the 30 P&Ls that lie underneath which is where the action is. And that's really the point of impact.

If that doesn't all come together in the way that it did in 2021, we're not in position in turn to do what we announced in November with respect to the spins, both with Healthcare and Power and Renewables. We're very excited about that move. Obviously, a decision the board took in concert with management, a lot of deliberation, but the response we got then and certainly subsequently gives us every confidence that's the right path going forward with these 3 individual businesses.

When we come into 2022 with a lot to do, certainly first and foremost we want to have another strong year financially. In our earnings call just a month ago, I think you heard us lay out a framework for us to drive strong topline growth, have that flow through from a margin, earnings and a cash perspective in a high-quality way. We put out a reminder to that effect on Friday you may have seen. I wanted to make sure, as we did at earnings, that everyone understood that these supply chain and these supply or these price/cost issues are real. You can see that. We're seeing that as we speak here in the first quarter, early in the first half, before our countermeasures take full effect. But no change. No chance in the environment, no change in what we see as hurdling in that regard.

We have been out over the last 3 weeks, we've had operating reviews with 3 of the 4 businesses, we'll head to Cincinnati tonight to see Aviation in the next couple of days, and just are really I think quite encouraged by what we see in the businesses. It's early and this is a company that tends to deliver easily 60% or more of its financial results in the back half. But the way we start the year I think is important. Had 2 weeks with Scott Strazik. Scott, as you know, runs our Power business, he's picked up responsibility for Renewables. If we bring what we call Energy Co together, I think the progress we made in Power, in Gas Power and by extension its gain in power conversion, continues to be strong. Clearly, the turnaround in Gas Power is something I think everybody appreciates. Between the exit of new build in the coal space and the EDF transaction, it becomes primarily a service play, which we had nice enhancement to that segment. Power Conversion, a business $1 billion in size, has really executed I think almost a classic turnaround here. We'll be in the low, maybe even the mid-single digit op margin range in 2022. It's relevant because we've got that team taking on some additional responsibility in Renewables.

A lot of what you've seen us due in Power, I think does play and is relevant in Renewables. We know we've got pressure in Onshore Wind in the absence of the demand we would have hoped to have seen in 2022, given the lack of renewal of the production tax credit. That complicates some of these price/cost issues, steel, logistics, and really pinched us where it hurts most, in our North American Onshore Wind business. But we're going to work our way thought that.

Certainly internationally, that's been a touch space for us. You've heard that from competition as well. That needs to be something we take better command of in terms of our upfront underwriting. We need to be more selective. We need to be more disciplined, let alone manage the price/cost dynamics, again, steel and logistics principally. And we'll do that. And I think when you look at what we should see in the first half versus the second half, clearly there is call it $600 billion plus or minus of incremental operating profit as a result of the countermeasures that we should see there in the second half of this year.

Grid is a business that is really going to be I think well positioned in the energy transition. Changing the generation mix is one thing, we've got to deliver it, that's where the Grid business I think is well positioned. We need to run that business well, better than we have. We're close to breakeven now. A lot of good progress in that regard. But there again, we can and should do a better job in terms of what we sign up for upfront, where Scott taking on responsibility for that business, I think, will give us an opportunity to accelerate that progress. Philippe Piron who has run Power Conversion has just picked up responsibility for Grid. A good bit of what we've done in PC I think will be something we can transfer and run at Grid. And there's a little bit of strategic opportunity there with respect to micro grids that we're going to explore.

Our Offshore Wind will come along. We've got $7 billion of commitments there. We know that has an exciting future ahead of it, but we've got to work it out first. Clearly, Julian, here in the first half, given the absence of the production tax credit and some of these price/cost issues.

We were in Florence, South Carolina just yesterday with our Healthcare business and that game is ready to go. Probably still a year out relative to the spin, but the way Pete Arduini, the new CEO, has come in, come back really because he started his career with us, he's hit the ground running. He's got a number of other changes afoot there. Just organically, both from a commercial and from an innovation perspective, lots of leverage in play on top of frankly robust demand we can't keep up with right now. But again, in different ways, the supply chain challenges we think will be increasingly clear as the year progresses.

I know we'll talk a good bit about Aviation, but we said at earnings and we reiterate today, high confidence that we've got a 20% topline growth opportunity here both in the aftermarket and with new units. As we see all of us returning to flight, with the crowd in the room, good to see that in addition to what our major airframer customers are telling us about their own production ramps.

A lot to do. A lot to do operationally which really is job one at GE here for 2022, while we get ready for the spin. We talk about that every day because we don't want anyone to think spins are more important than delivering 2022. But we're excited about the progress over the last several months with respect to the spins. Clearly, Healthcare is a little bit further out than the other two businesses. It's proven to be a talent magnet if I can go that far. Exciting about having Scott Reese come over from Autodesk to run GE Digital. That's important because he is an outstanding leader in the software world. He'll help us I think realize the full potential of that business. Also gives us an opportunity to move Pat Byrne over full time to look after Onshore Wind, some of the issues I just mentioned a moment ago.

Pete Arduini, again, new in role. He's just brought in Betty Larson from BD, a new leader in HR. Critical in addition to Frank Jimenez who will be the new general counsel for us as we prepare to launch. Frank joins us from Raytheon. A number of outstanding leaders we're excited to have on the team to compliment the team that we've got as we get ready, again, for Healthcare to be that leader in precision health, in diagnostics and therapeutics and in monitoring, pulling all the levers organically. And then hopefully, doing a steady stream of what we did last summer with BK Medical, the bolt-on acquisitions that enhance the overall profile of the company.

We know Aviation is poised. It's a multiyear run I think that awaits us both in the aftermarket and from a new unit perspective. But we're going to make sure we're ready for what comes next. You may have seen the announcement we made earlier this week with Airbus relative to a hydrogen demonstrator. We also recently announced a program with NASA relative to hybrid electric propulsion and that all comes on the heels of what we did with Boeing and United just a few months ago with respect to SAF. We don't how all that plays out, I'm not sure any of us do, but rest assured, when we think about an independent GE Aviation, the mission is clear. We want to continue to lead in the next generation of propulsion as we have over the last several.

And again, the energy transition, the feedback on the announcement has been strong. I think our customers are very keen to have us keep everything together because they know

the answers to their own energy transition challenges are uncertain, and the opportunity here for us to go forward with a strong on and offshore wind position, gas -- and yes, gas has a role to play here, in addition to all that we can do both with hardware and software with the Gird, I think sets up that business well.

We need to run certain aspects better, I mentioned that earlier. But all of these businesses really, I think, are going to go forward true to our purpose today of building a world that works. That will manifest itself in a lot of different ways, but I think importantly for shareholders, one manifestation is going to be at least $7 billion of free cash flow in 2023. So Julian, don't want to run on. A lot going on at GE. Coming off of 3 weeks on the road, excited about what we're doing, but we know we've got a lot of work ahead and we're on it.

Julian Mitchell: Perfect. Thanks very much for that, Larry. And maybe circling back to one of the things you said earlier about delivering on 2022, you had that update on Friday. Just trying to understand sort of did anything change or deteriorate versus what you expected in recent weeks? And those issues that were flagged in the Friday update, what sort of pace of improvement is dialed into your guidance for this?

Larry Culp: To be clear, it was not an update. I winced there. We were reiterating what we thought we had made clear and stated explicitly. I don't think we were convinced that everybody heard us, so we just wanted to get up on the soapbox and shout it a little louder. But no change in message and nothing new relative to what we had said just less than 4 weeks prior.

I think as we look at the first half/second half, it's important to remember that we are, for better or for worse, a back-loaded business. Working hard to change that, a lot of what we do from a Lean perspective is aimed at trying to smooth the year out, and smooth the months within a quarter out. But that's unfinished business. Just last year we had 60% of our earnings in the back half, I think '19 was profiled similarly. We're going to see that again, but for different reasons. These price/cost pressures that we referenced at earnings and re-referenced on Friday are real. I'm sure you've heard that from every company on this stage and there are a few more to come.

Our countermeasures there, both in terms of just buying better, redesigns in certain instances, are lagging the effect that we feel on the inbound invoices. But as we go through the year, we're going to bring onboard new suppliers, we're going to have redesigns that get us off the spot buy market, get us out of some of those more onerous situations. And at the same time, we're developing some better pricing muscles. We can't do that everywhere, and we don't have to. Some of our projects are longer term business, have escalators in them. Our service contracts, in many instances, have similar mechanisms. We get price just as normal course in those situations, but there's a bit of short cycle exposure where we've got opportunity to try to share some of this challenge. And I would argue that when you look at the order indices that we look at and in turn the backlog, we're making progress. I wish we were further along. As we go through the year, that progress upfront will build and in turn we should see more of it in what we're able to run through the P&L.

And all of that is related but I think separate from the supply chain issues. We talked about our Healthcare business. Healthcare is not the only business, but we'll see 300 or 400 basis points of revenue pressure here broadly on the company, because we just can't get everything we need to fulfill the backlog. And it really hurts in Healthcare, a bit because it is short cycle, a bit is from that demand is so darn robust. Be it public or

private spending, we see that coming into our order book. We know we've got an aging installed base that needs to be upgraded, let alone a number of new use cases. And that's all before we drive some of the commercial improvements that Pete and the team are working on.

There's a number of things that have to play out. It is what it is in this environment, but I think, again, I would just reiterate, after 3 weeks on the road, I have as much if not more conviction than we had at earnings that we know what we have ahead of us in 2022. A lot of self-help measures in motion. And as the year goes on, I think that will be more evident.

Julian Mitchell: Perfect. Then maybe taking a step back, free cash flow improvement. You talked about what's going on at GE. A few years ago, investors were worried that the conversion was too low from net income. Now it's the opposite concern that it's too high somehow. Maybe just to try and help people understand what's going on, you have a $2 billion delta of free cash flow operating income this year. What's driving that? And when you look out to 2023, you talked about the $7 billion plus, what kind of conversion is going alongside?

Larry Culp: Sure. Julian, as you know, and forgive me, I grew up in a neighborhood for 25 years where hot cash conversion was considered a good thing. And I still believe that. When I joined the company 3.5 years ago, it wasn't as hyper focused on cash in all its forms. I think when you look at where we are today, it's important to realize that we do have about $1 billion of a gap here, largely because the amortization which is there today and will be there tomorrow. CapEx and depreciation fundamentally in line. We're not managing it that way. I still think we can be more efficient with our Capex, but that's a different conversation.

As we go forward, particularly at this point in cycle, we know we have inventory opportunities. And I will not apologize to anyone for my zealotry on this topic. If the heart of a Lean transformation, and that's what we're doing at GE, you've got to get it right with respect to your material flows. Where a lot of waste is, where a lot of cash is, that's where you ultimately impact the customer for short lead times and highly reliable on-time deliveries. If you get that right, a lot of other good things will follow. If you don't -- right?

We've got opportunity. We're less than 3 turns today. If you think about a turn at GE, that's probably what, almost $4 billion of free cash. We're never going to apologize for that. In addition, as we think about getting out of our factory program and getting away from outsourcing receivables management to GE Capital, it becomes an opportunity. To do more than just chase past dues, but really think about terms rather than, if you will, back rating it and forgetting it. And that's all before we talk about the nature of some of our service businesses, where given the long term nature of contracts, we will get paid, we will get cash receipts, but we'll see some of that activity go through the P&L. And when you've got an Aviation business positioned where it is in the early stages of recovery, your cash receipts are going to run ahead of earnings for a little bit. And again, I think that's an attractive part of the GE model.

But all of that, again, is table setting. We want to drive strong topline growth. We want to expand margins at the same time and be an earnings-driven company complemented by all those cash matters. And as we move forward, have 3 companies that are not only investment grade, that have smart capital allocation strategies in place tailored to their circumstances. Capital allocation strategy is academic if you don't have a balance sheet to make decisions and put them into action. That's really, I think, what we've down not only

with the $87 billion of deleveraging, but what we're doing in changing the operating model and driving not only an earnings-driven cash flow stream going forward, but complementing that with smart but not excessive investments in working capital and CapEx.

Julian Mitchell: You mentioned capital allocation and I think the de-levering has opened up more optionality on cash usage. How likely is it that we will see GE do a large acquisition? Or is it a case of don't overload the businesses until they get everything set up?

Larry Culp: Well, it's a welcome change in the boardroom, Julian. Let me tell you, if you go not that long ago from worrying about all that we worried about to really having an array of options on the table, I don't think we're strictly looking at acquisitions. As we opened up, as we did, what was it, 2 weeks ago, with the board the array of options that we have from a capital allocation perspective, there's a lot that we can do. A large acquisition in 2022? I think at this point I wouldn't rate that as a high probability. If for no other reason than we want to make sure we get the spins out and comfortably with investment grade capital structures. That's job one.

But I would also at the same time say, don't be surprised if we rerun the BK Medical play in 2022. We were really excited to have an opportunity to bring that company to GE in large part because it fit so well with what we're doing in ultrasound, i.e., one of the best businesses we have within Healthcare. And to do that I think at a reasonable valuation. Good investment, strong strategic fit, but as importantly, it's a rep. The Healthcare team gets to go through the process of identifying what are strategic rationalization, diligence, integration. It's early. We're a little bit ahead of schedule in that regard. But if we can do a few of those -- but the point you made, Julian, is an important one. We're never going to do, regardless of how healthy the balance sheet is, first things first. If the team is consumed with the day job, and you might argue in Renewables by and large, that's what 2022 is going to be about, we really aren't going to ask them to do anything incremental or inorganically.

Julian Mitchell: In general, it's a very buoyant, or has been a very buoyant M&A environment. I'm sure the split news or spin news generated some sort of incoming interest from other parties about key assets. How appealing is some kind of alternative exit route for the assets with the separation?

Larry Culp: I think I got a lot more calls in fall of '18 when folks thought I might not make it than necessarily the fall of '21 when it was obvious that we would. Julian, I would say that we wouldn't rule anything out. This is a board that has been I think focused consistently on value creation. That said, there is a plan of record in place that we feel very good about. We might be able to complement it with a few bolt-ons along the way, but I think we're focused on the things that I've just highlighted and we'll see how things play out.

Julian Mitchell: One thing that you've been very keen on throughout your career is small corporate cost center, push the costs a bit (inaudible). The corporate cost issue at GE is still pretty large. On a cash basis it's $1.5 billion plus. Where does that number -- where should that end up?

Larry Culp: There are a lot of reasons you want a small center, and cost is but one. I think what we have found over the last several years is really managing from the bottom up just drives a much better degree of accountability. And in many respects, you could argue that a decentralized approach that we have been implementing is really what you see in the spins. We announced in November in many respects a logical extension of that strategy.

Not planned in that regard, but we feel strongly about it and all the more so given what we've seen in the last 90 days or so. That said, if you think about $1 billion of corporate cost today, I think we've shared publicly that as we think about 3 independent companies, they're all going to bring hopefully that frugal, small center mindset to bear. We'd say that we're probably talking, I don't know, $150 million to $200 million roughly per center, so you multiple that by 3. So that suggests that we've got another step down and that's a good thing. Takes us a little while, some might view it as cost, but that cost is rooted in a whole host of corporate functions that were built to serve a larger and even more complex GE. It's work that's easily done, it just takes a while if you will to replumb much of that infrastructure. But as we do that, we're going to set the businesses up to go on their own, but we'll bring some costs down that way as well.

Julian Mitchell: Then maybe switching to Aviation specifically, you brought that 20%+ revenue growth aspiration here. Maybe any color around commercial aftermarket expectations within that. Also, Military, where there has been a lot of issues for 18 months or so, where do we stand on that front?

Larry Culp: Yes. Let's take it in pieces because I think it's fundamentally coincidental that when we talk about 20% growth in Aviation this year, it's 20% in the aftermarket, it's 20% in new units. We know as we sit here today, departures globally versus '19 levels, down 20%. U.S. almost back to where we were at that time. Europe is down by 1/3 and China is down under 18%. With all of us here, we're poised and we know that particularly with CM, (inaudible), we're going to see a lot of shop visit activity. We're also seeing the sequential improvements as we speak. Unless something happens with the next variant that throws this recovery into jeopardy, we think that's really an execution challenge for us as opposed to demand.

I'm sure many people in the room have already heard both our major airframer customers talk about their production expectations for '22 and '23. We think we're well aligned, particularly on the narrow body side of things, and that is what yields the 20% topline growth there. Could the aftermarket be better? We'll see, but I think for now we'll stand by what we said in late January earnings.

Our Military business, terrific franchise. We're under winning where peacekeepers are in harm's way. We have some process issues, Julian, simply stated. These are not supplier issues, so we're not going to point the finger at anybody other than folks in the mirror. But I think what the team has done, to their credit, I'm really proud of them, we haven't; tried to muscle our way through this. It just gets some engines out a little bit more every quarter. Again, in the spirit of the Lean transformation, we said if we've got process capabilities issues, we need to drill to root cause. We need to fix it at root cause. If it takes a while, it takes a while. Full stop. But I know there are some who are anxious about what's happening. That's what's happening. We're going to through some of these process improvements, and I can go on and on. I won't. But I think as you look, as we look at the leading indicators relative to the bottlenecks and some of the other pinch points in our own facilities, our yields are up. In many respects or many instances our yields are up considerably. Our flow is improving. As we continue to work our way through the year, this will be less of an issue and we'll clear the backlog. Most importantly, be in a position where we've got more reliable on-time delivery and shorter lead times for customers.

Julian Mitchell: And then when we look at Aviation free cash flow, very good year last year. This year you've guided for it to be down a little despite the big aftermarket uptick. Any sort of context there?

Larry Culp: Yeah, I think the key thing to remember as we think about the year-on-year cash flow performance in Aviation is, our AD&A, our aircraft delivery payments, are a little bit out of whack. I think we all know that particularly with one of our customers, there has been let's just say some volatility in deliveries. It was a bit of a tailwind last year, it's a headwind for us this year. If we didn't have that dynamic, we would be up for the very reason you just cited. I think people who understand GE, who understand our Aviation business, know that that's a little bit of a timing dynamic. It's neither good nor bad, but there are going to be moments where it creates a little bit of noise. But I think as we get the MAX, primarily the MAX on a more normal production and delivery should, we'll be talking about this a lot less.

Julian Mitchell: If you look at sort of operating margins in Aviation, you have that sort of up to 20% medium term plateau at the height of the range. You already did a high teens margin second half of last year. What kind of -- what keeps that ceiling as it is?

Larry Culp: Well, I wouldn't say -- I hope we've never framed that as a ceiling. But I'd much rather deliver on a midterm target than necessarily raise that until we've demonstrated we can do that. That's just me, maybe it's wrong, but anyway. But that said, we know that as we talk about this new unit ramp, we're going to have some mix pressure. Early in let's say the LEAP's lifecycle, those new units are still money losers for us. Not outrageous, but we're probably not breakeven on the LEAP until call it 2025. So that's unhelpful. Clearly, some of the other supply chain issues that we've talked about, if you look at the Military example, we know we've got overhead that we aren't relieving as we work though some of those issues. But that's really the primary issue. But longer term, if we are positioned to do better all the while continuing to invest in hybrid and hydrogen and being fast, we'll do that. I think at this stage, we've got that target out here and we'll work our way towards it and do so in a way that's hopefully sustainable.

Julian Mitchell: Perfect. I know we're almost out of time, so please, if you have any time to pull up that audience response survey, please have a go at that. Maybe, Larry, just touching on the portfolio, Aviation will be the sort of core lamppost in a few years' time. When you look at the Aviation business itself, do you worry that it's too engine and commercial focused? Is there a need for some kind of rebalancing or greater balance with other non-engine products or on the Military side in the long run? And also, Aviation will have that long-term care assurance with it, what's best. What sort of appetite to try and whittle down that long term care business is there?

Larry Culp: Let me take those in reverse order. I think we're open for business. There's appetite from an LPC perspective and I think that even with the latest news we had in the 10-K, I suspect we're closer to a whittling down as you said. That may be in pieces. It may be in whole. But until that happens, it's on us to manage smartly and I think you've seen us do that both from an assets and a from a liability perspective. I love the fact the GE Aviation is the world leader in commercial propulsion, full stop. I think that's a beautiful thing. It's not the only thing that we do. We've clearly got the Military business, the better part of $4 billion in size that we're going to run better on a go-forward basis. Our Systems business, a couple of billion dollars there as well outside of propulsion. But I don't envision us trying to manage the portfolio in a way that investors could. If there are good businesses for us to be in, where we can apply our skills and drive returns, we'll do that. We won't try to be all things to all people, but in respect to Aviation and Aerospace, I think we'd be open to that. But first things first, I want to make sure we see our way through this recovery, through the launch of a GE that is Aviation centered. And that's what we're going to do the next couple of years.

Julian Mitchell: Great. Well, thanks very much, Larry, for you time here. Nice to catch up.

Larry Culp: Thanks, Julian. Thanks, everyone.