Sanford C. Bernstein's Strategic Decisions Conference
GE Capital

May 30, 2014
11:00 AM ET

Steve Winoker: Good morning, and thanks, again, for joining us with GE at this very last session of our Strategic Decisions Conference. Thank you for sticking me with through it. I appreciate it.

I'm Steve Winoker. For those of you who are new in the room, I'm the multi-industry and electrical equipment analyst and currently bank analyst for the next hour.

We are happy to welcome Keith Sherin, Chairman and CEO of GE Capital with us for the first time to this conference, following multiple years with Mike Neal.

GE Capital is now roughly about $374 billion in ending net investment, or about $510 billion in total assets. They have about $57 billion of tangible common equity, with roughly $7.2 billion of net earnings last year, and about $7 billion this year, and they run at about 11.4% on my last numbers tier one common, about 10.8% tangible common equity to tangible assets.

Management's targeting $300 billion to $500 billion of ENI by year end, driven by a combination of sales exits, including Synchrony, which is their U.S. consumer business that I'm sure Keith will talk about, as well as normalized returns.

Keith joined GE in 1981 through their renowned financial management program on the industrial side, became an auditor, then, had stints in engines and plastics before eventually being named CFO for all of GE in 1998. Keith was appointed Chairman and CEO of GE Capital last year following Mike Neal's retirement.

So, with that, I'll hand it off to Keith, and then for Q&A, I'm sure you don't need to hear this again, but you have the cards there to fill out. Send them up to me, and, hopefully, we'll be able to get through all of them.

(Video playing)

Narrator: I ask our customers what problem keeps them awake at night and Columbia Forest Products had a tough one. They make plywood and the panels look perfect when they leave the factory, but a company they sell to is demanding refunds, refunds for defects that only appear when the finish is applied. It's hurting their profits, so I offer to help. At GE Capital, we do a whole lot--

(technical difficulty)

(Video ends)

Keith Sherin: Great to be here. That commercial is part of our GE Access program, and I'm going to talk a little bit more about that as we go through the charts this morning.

There's really five key messages that I'm going to talk about as we go through talking about GE Capital today.

The first one is, we're really executing on the portfolio transformation. We're going to launch our Retail Finance IPO in the third quarter. We announced that last November. I happy to say it's on track, and, overall, we're targeting to get to the $300 billion of ending net investment, as Steve said, by the end of 2015. Part of that, the largest part of that, is the IPO and then the eventual splitoff of the retail finance business, and I'll cover that in a second.

We're focused on growing the middle market and the verticals where we have domain expertise and we have great competitive advantage. I'm going to talk to you about that. One of the big programs that we have that gives us that advantage is called Access GE, and I'll show you how we use that. We basically have opened up the resources of the General Electric Company to the customers of GE Capital Corp., and it really is a great partnership where we're helping our customers grow, helping them be more competitive, and it differentiates us versus the other competition.

Commercial volume was pretty strong in the first quarter. We're originating volume at good returns, and I'll show some of that. We're safe and secure. We have definitely transformed the balance sheet over the last several years. We've got a strong level of tier-one common capital, and $75 billion of liquidity. I'll talk a little bit about that as well. We've brought the CP down to $25 billion ahead of schedule, and we're probably issuing less debt than we originally planned.

And then finally, we're returning capital back to the parent. We've returned $13 billion since 2012 back to the parent and last week at EPG Jeff announced that we'll be doing $3 billion in 2014 while we continue to build out a world-class regulatory infrastructure, which is a tremendous amount of work for the organization.

So, just when you look at the picture of GE industrial and GE Capital, when we close the Alstom deal, assuming the Alstom deal gets done, we would be about 25% of the company's operating earnings, and, you know, we're a key part of GE Capital. We're going to be a smaller, more focused part but we're a key part of GE company.

We have a responsibility to continue to provide cash back to the parent to help with capital allocation at the parent level. That's a big priority for the leadership team.

We have a lot of competitive synergies between GE and GE Capital, as you know. We benefit from the rating of the parent, and it helps us with the cost of funds that we have as we borrow money and lend it on to customers. We get a tremendous amount of synergy between the industrial businesses of GE and the financing businesses of GE Capital, as you know, and the verticals, GECAS, GE Capital Aviation Services, Healthcare Financial Services, and Energy Financial Services, and we're growing our Oil and Gas vertical, as well.

We also have a lot of synergy. We work together at capital markets transactions for both the Capital business and the parent, and, finally, we file a consolidated tax return where our accelerated depreciation and borrowing charges help offset the pretax income of the company, and that gives us a cash and income annually that's quite substantial.

So, a lot of synergies. We're safe and secure. We're a senior secured commercial lender, and, even as we get smaller, we're still going to be a substantial part of the General Electric portfolio.

Here's the portfolio in Capital today. The numbers at the top, $380 billion of ending net investment last year. As Steve said, it was $374 billion in the first quarter. We had about $44 billion of revenues, and we made $8.3 billion of net income.

We-- the biggest business, and the core of GE Capital is the Commercial Lending and Leasing franchise. We're a senior secured lender. We're a leader in the middle markets, especially in the U.S., and growing in Western Europe. We're mostly a developed market enterprise. We need rule of law. If we're going to lend money, we want to get paid back, and, if we don't, we want to get our collateral back in a reasonable timeframe to earn our returns. And our underwriting approach is, we underwrite to hold it on book, and that's very substantial when you think about risk management.

In the middle, GE Capital Aviation Services, everybody's familiar with. We've got $40-- $38 billion of ending net investment. We're a leader in the industry, over 1,600 aircraft that own or manage. Just a tremendous franchise, and great synergy between GE and GE Capital.

Energy Financial Services -- similar relationship with GE, with the parent. We have great-- a big franchise in the renewable space. That's been very hot the last couple of years. We're growing our franchise in the Thermal business, and we're, as I said, working on expanding our Oil and Gas footprint.

Real Estate in the bottom left, we have $39 billion worth of investment in commercial real estate. We have $14 billion left in the equity book. We're running that off, and we're growing the debt book at-- we're putting capital to work at good returns. It's a senior secured lending business, basically, against commercial real estate, and we like the returns today that we're getting.

And then, the bottom right, the Consumer franchise. The largest piece of that business is the North American Retail Finance business, and we're going to work on the IPO and the splitoff of that, and I'll show you a little bit about that in a second.

So, really, a focus on middle market lending and leasing and things connected to GE.

We are getting smaller. If you go back to 2008, we were over $550 billion of investment. We've done a lot of shrinking. We've run off $100 billion of non-core assets since 2008. The team's done a really good job of making it smaller, more focused. Our big next transaction is the Retail Finance business, over $50 billion of investment.

Our focus is where we're advantaged in the marketplace, middle market lending and leasing, and I'll talk about our things that we think differentiate us versus the competition, and we have to improve our portfolio returns on capital efficiency as we exit the consumer business, and the whole team is focused on that.

So, $300 billion of ENI is sort of the target for the end of '15, and we'll get down to a 25% of the earnings of the company as we exit Retail and as the company acquires Alstom, a smaller, more focused GE Capital.

We announced the exit of the North American Retail business last November, and the team has just done just a tremendous amount of work on this transaction. The name of the company will be Synchrony Financial. You can see the total assets here, $57 billion, and $2 billion of income in 2013.

There'll be a separate pro form that will be filed with the registration statements we've filed with the SEC, and we're constantly updating that. We'll put the final updates in, in the next few weeks, and our objective here is that the IPO will occur early in the third quarter. I think we've received all the feedback we need from all the different parties that we're working with, with the exception of the final filings with the SEC to be prepared to go forward with this IPO.

So, we feel pretty good about this process. As you know, we're going to IPO about 15% to 20% of this business, and then we're going to have the remainder we'll own at GE Capital. We're going to run the business for however long it takes to prepare it to be independent as a separate public company, and when we complete that work, which will include capital levels, liquidity levels, as well as regulatory capability, we intend to split off the remainder, that 80% that we don't sell to the public, in a tax-free transaction, which is a share exchange with GE shareholders.

So, we will distribute the 80% or 85% that we don't sell in the IPO to the parent, and the parent will exchange that 85% or 80% of retail finance for GE shares in the marketplace. So, there'll be a tax-free exchange for our shareholders and, basically what will-- what that'll enable us to do, it'll offset a lot of the dilution from this transaction through a share buyback, and it enables us to hit the 9 billion to 9.5 billion dollar share count that Jeff has laid out as the objective for the company.

So, a tremendous amount of planning and a lot of work has gone into this. The team is really excited, and we're looking forward to getting started, so, I'm happy to say it's on track. This will be the last major step for us to get the company down to the $30 billion of ENI and 30% of earnings and 25%, including Alstom.

So, the focus, as I said, is going to be on the middle market franchise, leasing and lending to the middle market, senior secured. We're number one in the middle market sponsor business. That's been very active through the first half of the year.

Number one in equipment finance. The markets are pretty strong. We're seeing a little pickup in cap ex, trucking, construction, pretty good.

Number one in franchise finance, both fast food restaurants and low-cost service hotels.

Number one in healthcare finance. Number three in real estate debt. We do like the business, but we're pretty much in just the developed markets, and number four in corporate finance, and where we win are places where we have domain expertise so, that our teams know as much about the industry and the competitive dynamics as the business that we're supporting, as the customer we're supporting, and that we can help them to make decisions, allowing them to earn more profits, be more competitive, be more productive, whatever it may be.

We also have a direct sales force. We have thousands of GE Capital sales people who directly call on these customers, and that's a differentiating factor versus the banks, and one of the most critical factors is that people can count on us. When we go in and underwrite a transaction and say we can get it done, they can rely on us to get that done, so that's a big advantage we play on, all the time.

And on the right side are the-- some of the numbers about the Access program. We have over 600 experts inside of GE Capital, and inside of General Electric, who have-- basically dedicated people or volunteers who agree to work on customer problems. And so, our GE Capital sales team will bring in a customer problem, like you saw in the commercial, and we'll get engineers from GE or we'll get leadership help from GE, or we'll get finance help from GE or GE Capital, and we'll help the business team to solve their customer problem.

And we've had over 1,500 engagements. We've got over $11 billion of volume that we've enabled through GE Access, and everywhere I go, when I meet with our sales teams, and I meet with our customers, this is a great program that everybody really appreciates the work that they can get from GE. It's just a unique advantage to be able to tap into those resources of General Electric Company.

One other example that I just want to highlight about sort of the approach in the middle market that we're using is, we always talk about the verticals, the things connected to GE, GECAS Aviation Services, Healthcare, and Energy, but inside of our Commercial Lending and Leasing business, we're also vertically focused.

And what that means is that we have dedicated teams. Instead of being generalists from a sales force origination and underwriting and risk management, we've dedicated them by industry vertical. And this is just one example, the food and beverage vertical, and you're seeing more and more specialization by industry. We're going to go to 80%, 75% to 80% of our resources will be industry focused, as opposed to generalists calling on geographic territories with products.

And so, you could see that the-- we've got 11,000 U.S. food and beverage companies that are in the U.S. It's an incredibly big industry. We've dedicated our sales force. We've dedicated our risk teams, and our underwriting and origination teams, and we've brought in analysts from the banking industry who help to provide information about the competitive dynamics to our customers.

And over the last 12 months, you can see we've had a dramatic increase in our investment here, as a result of the success of being totally dedicated to this industry segment. So--

and it's across the products that we have. So, it's leasing. It's lending, as well as the sponsor business, and helping with different types of M&A, buy and sell side.

And we're building a lot of other verticals inside of GE Capital, because of the success of what we see here. So, we're building the oil and gas vertical, as I said. We're building forestry. We're building the metals and medical, and aerospace and defense, and you can just see some of the customers on the bottom. But this is definitely where the industry's going, not just in the U.S., but also in Western Europe.

The other verticals that we talk about are, obviously, the things connected to GE, and we love these franchises.

You can see the Healthcare Financial Services, $14 billion investment, 2.8% is the return on investment, and we provide financing for a lot of GE Healthcare's customers all around the world. We also do equipment financing for non-medical imaging equipment, for other OEMs and suppliers, and we've had a long partnership with Healthcare, and the team has got great domain knowledge, and is very highly respected in the industry. So, that's a big vertical focus for us.

Energy Financial Services, a similar relationship with GE Energy, GE Power and Water. We've provided financing for over 250 Power and Water projects in the last 10 years. We've got a similar footprint as GE Energy in where we do work, and we've had a huge program in the renewable space. We financed more than $4.5 billion, $5 billion of renewable products over the last several years, and we're expanding, as I said, into the thermal space, as the Thermal business picks up globally.

And then finally, GE Capital Aviation Services. Tremendous franchise, $38 billion of ENI, over 2% return, and customers all around the world, over 1,600 aircraft that we own and service. We've got a young fleet. We're constantly looking at moving the older technology out and investing in newer technology. We've got 80% of the fleet supports either GE or CFMI engines, so, this is a great franchise where there's just a tremendous amount of synergy between GE and GE Capital.

We're better off knowing the technical capability from the industrial business, and the industrial businesses are better off having this financing capability in GE Capital.

So, in terms of financial performance, these numbers haven't changed. We showed you this at the end of last year. $8.3 billion from continuing ops in net income last year. We're going to be about $7 billion this year. We've guided to $7 billion.

Two things that really are occurring. Number one, we have a lot less gains, just in Real Estate alone last year, with the transaction with Comcast when we sold our 30 Rock real estate, that was over $550 million of gains in one transaction. So, Real Estate gains are going to be lower, and, in addition, we're going to have a minority shareholder in the Retail Finance business for the second half of 2014. So, that'll have a little lower income for us on a total year basis.

$1.9 billion in the first quarter, on track for the $7 billion for the year.

Volume's pretty good. I'd say that it's very strong in the first half in Aviation. We've seen a pretty good pickup in the business. Very strong in Real Estate debt, both in North America and a little bit in London. And then the core equipment business, just Leasing and Lending, are probably mid-single digits. First quarter was tough from a cap ex perspective. A little bit of pickup in the second quarter, as you've seen from some of the other banks. They announced the same thing.

The portfolio quality is in great shape. Our 30-day delinquencies are really at very stable levels, I would say, and our common equity levels, as I said, are very strong. Tier one common at Basel I basis, over 11%.

So, the full-year guidance is on track. We haven't changed anything, and we're going to continue to execute on the portfolio transformation. That's the big priority we have.

And here's just a look at the future. As I said, you know, from a strategy perspective we're running the play to change the portfolio.

The big item is to execute on the IPO and eventually the splitoff of the Retail Finance business. You can see, that'll reduce the assets in the consumer by '15 quite substantially. We're going to grow the Lending and Leasing business. We're going to grow the verticals connected to GE.

In Real Estate, what's going to happen, we're going to continue to run off that equity book, and we'll invest in the Real Estate debt, as long as we can get the returns at the right risk profile that we see.

So, ultimately, our goal, as we get out past 2015 is to be about 25% of the company's earnings. We're going to have all the capital that we put to work with good returns above, obviously, our cost of capital.

We're building out the regulatory infrastructure. We have not been a bank, traditionally, and now we're regulated by the Federal Reserve, and that's a tremendous amount of activity for us, and our goal would be to pivot to growth in line with industrial. When we get to that new starting point, get down to the 25%, if industrial grows 5% to 10%, we can grow 5% to 10% and keep that ratio so that GE Capital does not become a bigger part of the company as we go forward.

So, middle market, connected to GE, and we're running the play on the strategy of the portfolio transformation.

So, Steve, that's what I had, and I'd love to go into the Q&A with you.

Steve Winoker: Fantastic, Keith. Come join me, and just to remind everybody, you can fill out those cards and they'll be brought up to me.

Let me start with a simple one.

Keith Sherin: Sure.

Steve Winoker: As a major lender, what's your view of the U.S. economy and the indicators that you track here, and then also in Europe? You tend to have a very rich data set. I assume you have a richer data set, in some ways, than when you were at Corporate.

Keith Sherin: Yeah.

Steve Winoker: How do you-- what are you seeing?

Keith Sherin: Well, it's-- there are a couple of pockets of things that are strong. I would say that for us, again, things that are connected to the portfolio, probably the strongest line we're seeing is in the commercial real estate space on the debt side. A lot of players have exited.

There is an opportunity to put capital to work at, you know, 75% loan-to-value at good returns, and that business has-- in some ways, it's relative to the volume they've done the last couple of years, as well, because we really clamped down on Real Estate while we were getting the equity book down to a size we like. Now that the equity book has got down to a size that is more manageable, in every sense, and continues to shrink, you know, we've allowed the Real Estate debt business to start doing some business.

So, they've got pretty good-- they've got a pretty good volume outlook. It feels reasonably strong.

Western Europe it's mostly London, I would say, is where we're seeing the biggest strength. A little bit in Australia from a commercial real estate perspective.

GECAS -- you look at-- obviously, you look at Boeing and Airbus and the number of planes that they're putting into the marketplace, the GECAS business is quite strong, from a volume perspective, and a lot of that is in the emerging markets. But that business is giving us quite a good volume lift.

I'd say Energy is relatively flat, year over year. There's a lot of investment in, obviously, alternative energy, but a lot of liquidity, as well. So, that's a little bit more of a tougher competitive dynamic.

In the core middle market, we are seeing a little bit of a pickup in cap ex. Two things that I think would be stronger than others. One is trucking, heavy trucking. We've seen quite a bit of strong volume in that business as people are re-fleeting. I guess they've deferred purchases, and there's new technology that's out, as well, that's helping, but that's been strong.

And construction equipment has been high-single-digit or double-digit, which is good. Maybe people are putting a little more cap ex to work and core leasing, you know, cap ex was slow in the first quarter, you know, low single digits in the core Leasing and Lending business in the first quarter, 3%, sort of volume growth, and I think that's a little bit better in the second quarter, but it's not dramatically different.

In the Consumer business, we've seen very strong consumer activity, especially a little bit higher percent on the charge card than on the total same-store sales numbers that you see, so that's been a good outlook.

Steve Winoker: Great.

Keith Sherin: Hopefully, that helps.

Steve Winoker: No, that helps a lot, because you're very close to that. So, Keith, maybe stepping back for a second, what are you changing at GE Capital under your leadership?

Keith Sherin: Yeah.

Steve Winoker: You know, given what you-- and, by the way, I imagine the view is very different this way than the other way. What--

Keith Sherin: I have budget arguments with Jeff Bornstein.

Steve Winoker: Right. So, what-- tell us-- just a little bit of perspective of what we should expect under your leadership from GE Capital?

Keith Sherin: Yeah, I think there's not a big strategy difference, obviously. We're executing the strategy that we agreed to with the Board of Directors and the leadership team. You know, we're going to-- we're going to get GE Capital down to about $300 billion of ENI, and we've decided to do that by executing the IPO and the ultimate split of the Retail business. So, there's real change from a strategy perspective.

I-- you know, from an ongoing execution, obviously coming from the finance side, one of the things I'm spending more time is on the commercial side, just to make sure I'm understanding what customer needs are, what our commercial teams need to be able to solve customers' problems, and how do they work through the GE Capital system. I think that's something I'm probably spending more time, because Mike Neal was just-- came up through the ranks, so that, so that commercial side of GE Capital.

So, that's something for me personally that's been great. It's fun, rewarding, and I'm learning a lot about how GE Capital operates. When you talk to the originations team about how do we solve a customer's problem through all of our processes.

The other side that I'm spending a lot of time on is on the regulatory side. It's something that I've had to learn what are the rules, and how do the rules apply to us, and then how do we satisfy those processes and things that we need to for the Fed. And that's taking quite a bit of my time, as well.

So, those are two things I'm spending a lot of time on. I've been meeting with all the-- I've met with all the businesses, met with all the commercial teams. Meeting a lot of customers.

And so, we're really-- we're really executing a strategy, and then we've got to run the place well, very efficiently and effectively from an operations perspective.

Steve Winoker: Well, it's interesting. You lived through the pain of 2008.

Keith Sherin: I'm happy to be here with you, actually, yes.

Steve Winoker: Well, but that put GE Capital in a certain light for you--

Keith Sherin: Sure.

Steve Winoker: --probably, at the time.

Keith Sherin: Sure.

Steve Winoker: And so, when you look at the risk versus growth tradeoff that gets made constantly in terms of what business you write--

Keith Sherin: Yeah.

Steve Winoker: --now, what business that team writes now, and historically one might have argued that at least sales had as much of a say as the risk side. Sometimes that goes back and forth. I mean, how do you view that balance and tradeoff now, culturally?

Keith Sherin: Well, there's so many things that are different today. I'd start with the number one: risk management process changes. The balance sheet is completely different. The funding-- you know, we've taken the commercial paper from over $80 billion down to $25 billion. We've taken the liquidity from $15 billion, $20 billion up to $75 billion. We still have the bank lines.

Just-- we termed out so much of the debt. You know, we were doing $70 billion, $80 billion a year of long-term debt. We're down to less than $20 billion a year is what we're talking about today.

So, the balance sheet is completely different, and the risk management mechanisms, the enterprise risk management around liquidity is incredibly strong, and that gives you a-- that is rule number one in financial services. You know, we could have done better, obviously, before the crisis, and today we have incredible mechanisms and oversight and processes around it.

So, that makes you feel great. From a risk management and underwriting perspective, you know, we've made some macro calls. We're just not going to be in the real estate equity business any more. You know, we're running that book off. We're not going to be in the consumer mortgage business. We still have the global mortgages that we're running off. We still have $52 billion of red assets, Steve, that are in run-off, and those are just places we're not going to go back again.

And then I would just say from a regulatory perspective, you know, the vast majority of things that you do to improve your processes, whether it's stress testing or, you know, stronger capital planning or different levels of risk management oversight, they're all really good practices, and those are all in place, and that includes governance all the way up to the GE Capital, up to the Board of Directors from GE Capital's team, up to the risk committee of the Board of Directors and the full Board of Directors.

So, so many things have changed, I think. I think number one, liquidity, and everything around the balance sheet management. Number two, clear definitions of what we aren't going to do, which were at-risk areas that were deemed too risky and proved to be too risky as you look at the stress they put us under, and then, number three, just tremendously different processes, I would say, about everything around capital planning and risk management, enterprise risk management.

Steve Winoker: Competitively, I mean, is there a degree to which the remaining business that's still green is-- I don't want to use the wrong words here, but maybe held back a little bit from growth that otherwise they'd be able to be more aggressive out in the marketplace as a result of still being part of GE, and, you know, the-- what must be massive risk aversion, given what you went through?

Keith Sherin: I-- the green businesses, you know, it's really more tied to the economic outlook, as opposed to that we're holding any green businesses back today. You know, the-- if you look at the last five years, and all the targets we set out, we've basically exceeded the shrinkage targets year after year after year. So, the originations and the-- have not caught up with the collections and the refi and the run-off of the red assets.

And so, I-- you know, there's been no pressure, really, to hold the green business back from a-- you know, capital allocation. There's pressure to-- you know, like in GECAS, we have asset concentrations with certain customers or in certain geographies that we're just not going to beyond those. But really we're not holding back any of the mid-market lending and leasing just based on capital allocation.

We actually have built up quite a bit of capital. We have excess capital. In the end, you see what's happening. The cash balance built up, and it's not really that efficient.

Steve Winoker: Right.

Keith Sherin: You know, it does affect your margins a little to have all that excess cash. So, we have capital and we have cash to put to work, and none of the green businesses, I would say, are really being held back for that. It's really the economic outlook, and it's been M&A. We haven't really seen people part with assets for quite a while, but, hopefully, that'll pick up, as well, as, you know, the European banks go into the stress test, maybe we can find some more things where they'll be parting with assets at prices that-- we've been very disciplined. If their pricing is right, and the risk side is right, and we get the returns we want, we can put that capital to work.

Steve Winoker: I mean, since you're mentioning it, do you have a preference, geographically for where you would pick up assets, assuming the right price?

Keith Sherin: Well, the main preference is developed markets. You know, other than GECAS, the rest of GE Capital is a developed market business, and so, right now in the U.S. would be very attractive for us. It's a-- we love doing business here, and it's just there aren't a lot of, you know, inorganic opportunities, I would say. In Europe there are more inorganic opportunities as the banks are sorting out what level of capital and liquidity they need, based on the upcoming stress tests, and the requirements from the regulators.

So, those are really, Western Europe and the U.S., North America, a little bit of Canada, maybe.

Steve Winoker: And in terms of returning to growth--

Keith Sherin: Yeah.

Steve Winoker: --since we're, obviously, on this kind of path of discussion, what-- you put on the slide 2015, basically flat, with Synchrony, you know, adjusted for Synchrony.

Keith Sherin: Well, it'll get down to the $300 billion in 2015. We're going to be above that in 2014, because we won't have the splitoff or the full run-off yet.

Steve Winoker: But the other businesses are growing.

Keith Sherin: Yep. Yep.

Steve Winoker: And so, for the whole thing to start growing, as you said, future, but is that really--

Keith Sherin: It's past 2015.

Steve Winoker: Okay. I mean, any reason to believe it would be extended beyond 2016?

Keith Sherin: Well, you know, we'll see. I think that's-- that's the future, and we have quite a bit of execution to do to finish the IPO and the splitoff, and then I think you revisit it at that point, right? That's where you would take another look. We've laid out what we're talking about, maybe, for 2016, but we're still in early 2014.

Steve Winoker: Right, right, right.

Keith Sherin: So, I think, you know, what I would say is the Board wants us to execute the plan that we've talked about, execute the Retail IPO, execute the splitoff, ex that, get down to $300 billion, and from there, you know, we'd have another conversation about, okay, now where do we go here and why?

Steve Winoker: One of the investor questions from the audience, a great question here, now that competitors like CIT are back on track, can you discuss both turnover and competition in the industry?

Keith Sherin: Yeah, I think there's no real place that doesn't have challenging competition, and, you know, whether it's the traditional larger banks, or it's other finance competitors like CIT, or new competitors that come up from, you know, the hedge funds or private equity, you know, there's plenty of competition out there, and that's why we need to differentiate ourselves with things like Access GE.

So, I-- we don't have anywhere-- low interest rates, lots of liquidity create very challenging competitive dynamics, I would say, and that's the reality of the marketplace that we have to deal with. So, we have to differentiate ourselves with the domain expertise and bringing something extra to the table instead of just capital.

And so, those are realities we have. I don't think there's anything that's really easy about competition in financial services today. And that's why you need to differentiate yourself.

Is that all right?

Steve Winoker: Yeah, no, that's good. And let me continue to move through some of these investor questions. So, based on comments in your presentation alone, it appears Synchrony-- well, once it's gone, it's a significant amount of assets. It's something like 50% of assets, 28% or so of earnings. If that's correct, how are you going to deal with the earnings dilution on the GE Capital side.

Keith Sherin: Yeah, on GE Capital, we're not. We're going to be smaller, and I think as you saw, Jeff Bornstein and Jeff Immelt have laid out sort of the framework that-- for GE in total, part of the offset to the loss of Synchrony earnings is the benefit of the buyback that we effect with the splitoff of the remaining 80%. I think it's around half of the dilution, and the rest is going to come through simplification and other cost-out efforts through the entire company.

But in GE Capital, that will be-- we will be smaller. We will earn less, and we will-- that's part of getting to 30% or 25%. We will be smaller.

Steve Winoker: And a related question from the audience, GE has an SG&A cost reduction program. You just mentioned simplification. What's GE Capital doing to reduce its SG&A and increase its efficiency?

Keith Sherin: Yeah, we have a simplification. We're participating in the same programs that GE, obviously, is leading. It's a huge cultural change. It's not just a cost-out program. For us, we have about $11 billion of SG&A. You know, we are continuing to take and reduce the number of profit and loss centers we have, so aggregating things at a little higher level.

We're doing so much more in shared back offices, and, you know, Jeff Bornstein led the way in GE Capital. We're doing that across the industrial business today, and there's more we can do in GE Capital on that model to just have, really, the businesses be more product lines with great distribution and commercial front ends, but all of the processing be done in centers of excellence, with common resources.

And so, we're going to do a lot more standardization there, and the partial offset to that, I would say, is that we're spending a lot more on regulatory excellence and IT as we, you know, get the systems and processes in place to meet the requirements that we're going to be held to.

So, we're continuing to streamline everything on the core business. We will also be exiting non-core portfolios, and that just adds complexity. When we have some of these things that are sub-scale that we've had over time, and as we run-off those red assets and exit the sub-scale and non-core portfolios, that also will help with some of the SG&A and simplification, Steve.

Steve Winoker: Are you ending up with stranded costs with the Synchrony IPO, once that's gone?

Keith Sherin: Well, just based on the fact that it is a very profitable business and a significant part of GE Capital, we're going to have to do a substantial amount of simplification to be able to deal with the loss of that business, in terms of what it absorbed from an overhead perspective.

So, I can tell you, that's one of the big focus areas I have. It's one of the focus areas that both Jeff and Jeff have with me as we develop the plan for ultimately not having Synchrony as part of the portfolio. What are we going to do with those excess costs at headquarters? And we've got to change how we process things to be able to get ready for that.

Steve Winoker: So, it's not something that you can do in advance, or is it concurrent?

Keith Sherin: Well, we're starting. Sure, we've got-- we're doing the planning, and we're looking at it. Again, it's less-- fewer P&Ls, more consolidated back office and centers of excellence for shared work, and then-- and changing how we operate in terms of investments in IT to be a lot more streamlined and efficient.

So, yeah, we're doing-- we're starting it now.

Steve Winoker: And so, would it be-- the financials be timed such that if, say, the 80% that goes next year in 2015, after the 20% this year--

Keith Sherin: Yeah.

Steve Winoker: --or 15% to 20%, is that-- the cost reduction you'd expect to be concurrent with that second set of actions, so that as you deconsolidate I won't see a ton of extra costs on this?

Keith Sherin: It won't be-- it will be ongoing through the period of preparing Synchrony to go out, but, you know, hopefully, by the time we get there that we'll have already dealt with most of the actions to not have it be a problem. But it's not a cliff amount. It's going to be just a steady-- sort of, just the way Jeff Bornstein's described it, a steady state of restructuring and process change to reduce our SG&A, while we get ready for not having Synchrony.

Steve Winoker: Okay. There's a related question here. How is employee morale in a division that's shrinking in importance to GE, and are there employee retention issues as a result of that?

Keith Sherin: Yeah, it's a great question. It's interesting. Margaret Keane and her team run the North American Retail business. They're fired up. They're really excited to be able to go out and create a separate public company. They run a great business with great customer relationships, good value proposition, and we've had GE and GE Capital people join that team, looking forward to sort of the new experience of becoming a separate public company. And so, I think the morale there is excellent. It's a tremendous amount of work.

Inside of GE Capital, I feel like the morale is very good. You know, we're investing in growth, and we're investing in regulatory excellence, and, at the same time, we're streamlining other things. So, there's a balance, I think, of activity going on.

You know, there are some businesses that are-- like the U.K. home lending business. It's not strategic. It's in the red asset category. It's been there for years. So, people-- they know it, and what they're asked to do is do a good job, run the place effectively, and they know their role, and they know what role they're playing in.

So, I think that for places that are in the red assets, we're clear as day about it. We don't tiptoe around it. We say you are-- you are in the run-off category, and we're going to continue to downsize it as much as possible. So, the people who are there understand their role, and understand the place they fit strategically.

But it's something I-- you know, we have to think about all the time, making sure we don't lose our good employees. So far, our turnover has been very low, and, as I said, we're adding a lot of people, a ton of people, for the regulatory side.

Steve Winoker: On the consumer asset side, why not package all of consumer in this IPO instead of just the, you know, the pieces that you took?

Keith Sherin: Yeah, I-- it's an interesting idea. I think it's a little-- it's just a little too complicated to really execute this with certainty, high certainty. You know, the other consumer assets, obviously, the run-off assets, really wouldn't be that attractive to this business. To throw in some U.K. home mortgages or the French mortgages, it just isn't something investors are really going to be interested in, is sort of our view, and the complexity of adding those international assets to something that we want to have be a successful company and be able to develop its own regulatory capability, it really was just too complex for them.

So, you know, it was what's doable, what's the fastest path to getting and executing the strategy, and what would investor, really, appetite be for these things. So, I-- it just was determined to be too complicated and less efficient and less desirable, I would say, from an investor perspective.

Steve Winoker: Okay, great. A couple audience questions around interest rates.

Keith Sherin: Yeah.

Steve Winoker: First, I guess these are both the same question. What is the sensitivity to interest rates for GE Capital, say 100 basis point move higher in the 10-year, what impact would that have--

Keith Sherin: Yeah.

Steve Winoker: --now and over the long term?

Keith Sherin: Well, as most of you know, we're match funded, so, our basic principle is that we, you know, fund our fixed-rate assets with fixed-rate debt, and our floating-rate assets with floating-rate debt. We do have some sensitivities about earnings at risk for a 100 basis point move. It's actually a slight positive if we had a 100 basis point parallel move and nothing else really changed. We have a little bit of a gap where we've funded out some of our long-term debt, and we're prepared for higher interest rates.

So, it's less than a couple hundred million dollars, I would say, on a pretax basis is sort of the analysis we do on a 1% move, a 100 basis point move on interest rates.

Steve Winoker: That's helpful.

Keith Sherin: Yeah.

Steve Winoker: A question here around, for example, your Oil and Gas vertical, asking about, well, what financing are you doing? Are you financing pipelines, downstream, upstream, exploration, appraisal, what geographies? And I think the point is, to what extent is to what extent is this-- does this raise your risk profile?

Keith Sherin: Yeah. I think in Energy Financial Services, we've been in oil and gas for a long, long time, and we do finance known producing developed wells, oil and gas, and the team has a tremendous track record on that. So, that's a business they've already been in. We also have quite a large midstream business with pipeline infrastructure and distribution infrastructure assets.

So, that's not really changed, and I think we're looking at, can we provide more equipment financing and lending to some of the alternative energy spaces, things like LNG in a box, the clean energy JV we have, you know, are those things that we can provide financing to in the Balkan and stop the flaring of gas, and, is it an opportunity for us to do some more equipment-based lending.

So, those are the kind of things. From a risk profile, probably the bigger risk would be in some of the oil and gas reserves that we've done, but we've got a long track record of them. We're not changing the profile on that.

Steve Winoker: Okay.

Keith Sherin: Yeah.

Steve Winoker: A couple questions around real estate. Any internal contemplation of spinning it off as a REIT, as opposed to triggering taxable gains or offset with restructuring?

Keith Sherin: Not at the present time, I would say, and if you look at our, you know, our reporting on the Real Estate equity book, as I said, it's about $14 billion, it does have a couple billion dollar embedded loss in it, if you were to mark it to market today. We don't do that. It's an asset held for long-term, and we believe that over time, as we execute on whatever the property plan, whether it's cap ex, or it may just lease up, it may be rent growth changes over a period of time, you know, we believe that we'll more than recover our value.

So, you know, to just do it in a one-shot move we think would destroy value. And so, not at this present time, we don't have a plan to do something like that.

Steve Winoker: Okay, fair enough.

Keith Sherin: Yeah.

Steve Winoker: I think a broader question here. For the non-direct industry vertical businesses, so, Commercial Lending and Leasing that's left--

Keith Sherin: Yeah, yeah.

Steve Winoker: --it may be helpful-- because I know you tried to address it in the presentation, as well, but what's true about Commercial Lending and Leasing that's not true about Consumer with regard to the real overlap with GE's current industrial businesses? So, you sort of say from a synergy perspective you described some of this at a high level--

Keith Sherin: Yes.

Steve Winoker: --but help folks understand sort of why CLL-- people take the other bit for granted. Like, okay, I can understand GECAS--

Keith Sherin: Yeah, yeah, right, right.

Steve Winoker: CLL-- GE is not in those specific businesses.

Keith Sherin: That's right.

Steve Winoker: So how do you-- maybe help people understand what's different about it.

Keith Sherin: Well, for us, we think it's a-- they are industrial customers, and they are businesses that operate, in many ways, a lot like a lot of the GE franchises themselves, and, so, while there's not a direct synergy like there is with the Aviation business where we have the technology advantage from aircraft engines, you know, our ability to provide them with help, whether it's technical things from a technology or operations or manufacturing capability like you saw in the commercial, or even leadership practices or maybe treasury practices. Who knows what they are? You know, we-- whatever those things are, we're able to bring some more value to these customers that just a bank wouldn't be able to do.

But there's not as much direct synergy between GE, and we don't try to pretend there isn't. We say there are things that GE can bring to that customer base that help us to compete versus the banks, but it's not that really, you know, franchise finance isn't there because we're in the GE industrial business. We wouldn't say that, Steve.

Steve Winoker: I mean, look, it's a good business on its own.

Keith Sherin: It's a good business on its own.

Steve Winoker: Access GE, which you described, is-- how big-- I mean, you gave us a few numbers, but in terms of the investment in Access GE, not the GE Capital part of it, but the GE industrial part of it?

Keith Sherin: Yeah, it's in the tens of millions of dollars. You know, we're-- a lot of the teams volunteer to do it. You know, I just recently did one with the CFO of the Transportation business with a CFO of an automotive company, and, you know, he just wanted to get some understanding of how we were dealing with information to provide better forecasts on warranty costs. And so, we took a look at the model for the locomotive business, and everything we've done with our service business there, and we were able to take that CFO and help him with sort of what we did, from a process perspective. And that's a part-time job for the CFO of Transportation, but he loves dealing with the customer and helping GE Capital.

So, a lot of those resources are part time, and they're just helping, but there are-- but, you know, it's tens of millions of dollars of dedicated resources who are fully-- full time on it.

Steve Winoker: And now that you mentioned that, it makes me think of the Industrial Internet initiative and I think there's-- I forgot the latest terminology, but Industrial Internet initiatives on the GE industrial side.

Keith Sherin: Yeah.

Steve Winoker: Within GE Capital you have a tremendous amount of access to data, as well, across your customer base. Is there any linkage that you have on the Capital side?

Keith Sherin: There are-- yeah, there are programs in GE Capital, and I think we can do more here. Clearly, the Retail Finance business and the data that we have about customer behavior is incredibly important to our retail partners, and we're mining that data, and we're using a lot of that information to help our customers be more competitive and grow their sales better.

On the rest of GE Capital side, there are-- we're just starting now to, I think, to provide better decision-making information off of that data. You know, our-- I was just out at our Fleet business. We have a great Fleet business, providing trucks and cars to lots of the large industrial companies in this country -- telecom companies, everything.

And the ability for us to tell them how their fleet is operating, what their costs are, how they could change those costs by comparing to the rest of the database is quite an advantage. And so, we're just now getting started. We're actually working with Bill Ruh in the software center at San Ramon and our Commercial Finance businesses in the CLL-type space. Not so much on the Real Estate side, not so much, really, on the Energy side. They are really just investments, but I think the CLL, the core part of it, will be a place where we can use that data and help our customers, Steve.

Steve Winoker: That'll be interesting to watch.

Keith Sherin: Yeah.

Steve Winoker: So, more specifically, return of capital expectations.

Keith Sherin: Yeah.

Steve Winoker: And so, Jeff, I think, laid that out last week for this year, right? But how do you see that developing over time in terms of special versus income dividends, when you get past-- there's a bunch of excess capital, we would argue, there.

Keith Sherin: Yeah.

Steve Winoker: So, you're still targeting 11% to 15% ROE, is that right?

Keith Sherin: On a tangible basis. We had 12% to 15% we put on the chart.

Steve Winoker: Sorry, 12% to 15% now. So, how much excess capital do you think there is, mathematically, and how many years might it take, or how should we investors think about how long it takes to see that go up to the parent?

Keith Sherin: I would say that in the near term what you should think about are profiles that are more like 2014. You know, I think we're going to-- we're going to probably be paying about 30% of income dividends as a baseline, as an objective. I think that's pretty much an industry standard in the Fed-regulated world.

You know, we don't have the ability to do the buyback program. So, those special dividends are essentially what you would compare to the bank's capital allocation as their buyback. I don't think those are going to be dramatic in the near term, because, you know, we're going to build out those regulatory processes.

I think, as you said, from a quantitative perspective, we feel great about our capital levels. But we've only been in the Fed system for two and a half years, and we're building the qualitative processes, and so, I don't think you're going to see a dramatic change from sort of the 2014 profile in the near term.

And so, you know, for me, we've got to execute, as I said, a strategy to move the Retail Finance business out, get through 2015, get down to the $300 billion, and then see whether or not we're, you know, meeting those regulatory standards to be able to get at some of that excess capital. I wouldn't count on it in the near term, you know.

Steve Winoker: But the historical desire was to have GE Capital contribute at the same dividend level as the parent.

Keith Sherin: Sure. Sure.

Steve Winoker: Was giving the shareholders that--

Keith Sherin: And I think you're pretty close to that in 2014 when you look at the regular and the special.

Steve Winoker: The combined, yeah, and going forward. And so, going forward, we should think about, you saying, 2014 profile income and special, going forward, or just income?

Keith Sherin: I don't have a final answer on it. We end up doing a capital plan every year. I said that would be a good profile, I think.

Steve Winoker: Okay.

Keith Sherin: Yeah, I think the-- again, we need to do that every year and go through our processes. But that's-- it's not going to be a more aggressive profile, I can tell you that in the short term, Steve.

Steve Winoker: You mentioned on one of the slides about 2% ROIs on, I think it was newly written business.

Keith Sherin: Yeah.

Steve Winoker: I mean, how is pricing developing now? Maybe it's more about what's the trend and trajectory?

Keith Sherin: Yeah. Yeah, I'd say that both CLL in the U.S. and in Western Europe and Australia, Japan, was about a 1.8% ROI in the first quarter. So, we're-- you know, we're seeing-- I think it's down from 1.9% last year. So, there's a little bit of competitive pressure there.

If you look at Real Estate, that's around a 1.8%, a little higher ROE with some of the leverage there. GECAS-- and that's pretty steady, I would say, the Real Estate. GECAS is pretty good, over 3%, EFS over 3%. Those businesses have been able to underwrite at pretty good returns, but, again, as I said, GECAS pretty strong volume, EFS relatively flat.

Steve Winoker: And net interest margin, I think, was about 4.9% in the first quarter?

Keith Sherin: Yeah from 5%, yeah.

Steve Winoker: So, it was a slight, 11 basis point, decline. But going forward, I mean, would you expect the 5% level to be the right number we should about, or?

Keith Sherin: Well, I think you've got to adjust it for the mix, obviously, of the Retail Finance business. I think, you know, really we're going to have to start separating what's the Commercial level, and what's the Retail Finance level. And we showed you some of those metrics in total, but, you know, around, you know, 4.8%, 4.9%, 5%, somewhere around there.

We're being very disciplined on that capital allocation for new margins, and that's served us well.

Steve Winoker: Is that post-- that 4.8%, 4.9%, post Synchrony?

Keith Sherin: No, no, no. That's today. Synchrony will-- I forget what the chart-- it brings it down somewhere in the 3%.

Steve Winoker: 3%?

Keith Sherin: Yeah.

Steve Winoker: Okay. And that's helpful. And maybe-- we're just about out of time here.

On the tax side, one other question, you guys have historically run, I think, about $400 million a quarter or so of structural tax benefits that we've talked about.

Keith Sherin: Right.

Steve Winoker: How does that shift, now, going forward?

Keith Sherin: Well, obviously, a large portion of that is related to the active financing exception there, sub-part F, and we need to get that renewed. That's in the extenders package. We have broad, bipartisan support for that, but it expired at the end of 2013.

We have a November calendar year, so we-- basically through 2014 in November we're under that existing regime, but we need to get that renewed. Last time it got renewed, it got renewed after the end of the year, so it may be a similar profile to that, depending upon how active Congress is in, you know, resolving the extenders.

So, that's the biggest piece, I would say, to that. But, you know, if that's renewed the way we expect it to be, you're going to have a similar profile going forward of a-- you know, right now we're talking about a mid-single-digits tax rate as we execute the Retail split.

Steve Winoker: Great. Okay, so I've run out of time, but are there any other comments you'd like to make?

Keith Sherin: No, it's great to be here. Good to see you.

Steve Winoker: Nice to see you at GE Capital now.

Keith Sherin: Thank you, Steve. Thank you. Appreciate it. Thank you.

(applause)