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EDITED TRANSCRIPT

GE - General Electric Co Company Update

EVENT DATE/TIME: JUNE 26, 2018 / 12:30PM GMT

OVERVIEW:

Co. provided an update on its fundamental changes.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the General Electric Company Update. (Operator Instructions) My name is Ellen, and I will be your conference coordinator today. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to turn the program over to your host for today's conference, Matt Cribbins, Vice President of Investor Communications. Please proceed.

Matthew G. Cribbins - *General Electric Company - VP of Investor Communications*

Good morning, and welcome to today's webcast. I'm joined by our Chairman and CEO, John Flannery; our CFO, Jamie Miller and GE Healthcare CEO, Kieran Murphy.

Before we start, I would like to remind you that the press release and presentation have been available since earlier today on our investor website at www.ge.com/investor. Please note that some of the statements we are making today are forward-looking and are based on our best view of the world and our businesses as we see them today. As described in our SEC filings and on our website, those elements can change as the world changes.

And now I'll turn the call over to John Flannery.

John L. Flannery - *General Electric Company - Chairman & CEO*

Good morning. I appreciate the opportunity to speak with you today and discuss some important developments that we announced this morning. We are making fundamental changes to position our businesses for the future and redefine GE for another century of success. As you know, we have been working to determine the appropriate longer-term strategic focus for GE. There are 3 essential elements of this strategy: one is focusing our portfolio for growth and shareholder value creation; the second is strengthening our balance sheet; and the third is a market shift in how we run the company. With respect to our portfolio, our Aviation, Power and Renewables businesses will be the core of GE going forward. These are 3 formidable franchises where we've built leadership positions over many decades. These businesses also have significant strategic linkages. They share technologies, digital and additive strategies and business models. While our core Aviation, Power and Renewable businesses can thrive inside of the current GE framework, we think substantial value can be created by moving other businesses outside of GE. To implement that strategy, we are creating a separate stand-alone Healthcare company and we also intend to fully separate BHGE. These are 2 strong and competitive businesses with leading positions and strong growth prospects but they both have various constraints operating inside the current GE construct. We believe these businesses can achieve greater results for employees, customers and our owners as stand-alone companies.

The pending merger of our Transportation business with Wabtec was driven by the same strategic approach. We will begin the process of separating our Healthcare business immediately. We will monetize approximately 20% and approximately 80% of Healthcare will be distributed tax free to our shareholders through a spin or split. Kieran will share more with you on Healthcare later in today's presentation.

Oil & Gas was separated from GE in July of 2017 when we made the strategic decision to combine it with Baker Hughes. There's strong industrial logic for the transaction, the companies are much stronger together and shareholders are getting the benefit of significant synergies both on the revenue and cost side as well as benefiting from substantial combined technology. We expect to pursue an orderly separation of the company within 2 to 3 years with a focus on maximizing value for BHGE and GE.

Strengthening the balance sheet of the company is a top priority for us. This will allow us the flexibility and capacity to invest in growing our core businesses going forward. We will reduce our net debt by about $25 billion and this will bring our net debt-to-EBITDA below 2.5x by 2020. We will run the company with a substantially higher cash balance and reduce our use of commercial paper.

Our strategy with regard to GE Capital is clear, we're making it smaller and more focused. We are reducing assets by $25 billion and we'll bring our debt to equity to less than 4x by 2020. We are aggressively working on actions and alternatives to mitigate, reduce or eliminate our exposure to long-term care insurance.

As I outlined at EPG, we will run GE Company in a fundamentally different way going forward. Our businesses will be the center of gravity and will run on a new operating system that we believe will improve our operations and cash performance. These changes will reduce corporate costs by at least $500 million by 2020. We expect this number to grow over time as this velocity is applied across all levels of the company. This is in addition to cost actions already announced in 2017 and 2018.

Lastly, we also announced this morning that Larry Culp will succeed Jack Brennan as lead Director effective today. Jack has led us through significant change in the company, including a leadership transition and I want to thank him deeply and personally for his service. I'm excited to work with Larry; and his experience fits extremely well with the changes we're making at the company.

In conjunction with previous actions, today's announcement marks the emergence of a new GE, a high-tech industrial GE. A simpler, stronger and more focused company at the core, a strengthened balance sheet, a new operating system and a bright future for our Healthcare and BHGE businesses. This is a GE that is equipped to fight for the future.

Now I'd like to cover in more detail our changes to the portfolio, including the core GE going forward, and our plans for Healthcare and BHGE. I want to talk about the philosophy and strategic intent behind these decisions. As I've said previously, the steps we're taking are really a means to an end, the end being a simpler, stronger and more focused company where our quality assets can reach their true potential and flourish in the decades ahead. We sought to position the businesses in an environment guided by 4 basic principles: the maximum ability to pursue their organic and inorganic investment strategies; strong alignment for management incentives linking performance and reward; reducing complexity and cost, while improving decision-making speed; and making sure any central essential services are subject to a market test by the business units. We are fundamentally inverting the company to make the business units the center of gravity. I want to focus the businesses externally into the market. We'll have a much smaller corporate focused on strategy and execution, capital allocation, talent development and governance. The entire fabric of the company will be one of continuous improvement driven by operating leaders using well-proven tools, like Lean and Six Sigma. Digital and Additive strategies will continue to drive customer value and performance. We believe that these changes will yield substantial improvements in performance over time. There will be improved focus, better accountability, clear capital allocation decisions, more strategic optionality and better alignment of compensation. Our plan will create a strong, exciting and growing GE built on operational execution and robust industrial logic. Going forward, GE will be comprised of Aviation, Power and Renewables, supported by Digital, Additive and the financing expertise of GE Capital.

These are leading businesses solving the world's toughest problems for our customers. By combining these strong franchises with a healthy balance sheet, we see numerous avenues to invest for growth. We see sustained strength and growth in Aviation going forward. We see growth in the overall Renewables market and in our expansion of market share into new areas, like offshore wind and storage. We see earnings growth in the turnaround of our Power business with 1/3 of the world's electricity from our installed base and 2 of every 3 flights on our engines, GE is a high-tech industrial company that forms the backbone of a connected and electrifying world in every sense of those words. In addition to the strength of GE going forward, we're also unlocking substantial value for our shareholders. GE Healthcare is a leader in the drive to more effective and more efficient health care outcomes. BHGE is uniquely positioned across the value chain as a full stream, oil & gas company. Our merger with Wabtec creates a global leader in the rail industry. As focused pure plays, they'll have greater strategic flexibility and more resources to pursue strategies dedicated to their industries.

I want to spend a minute touching on each of these franchises. Our Aviation business is a market-leading business with industry firsts spanning back decades and our technology stack has never been stronger. Both the commercial and military businesses are strong. Our fleet is young, with 61% of our engines not yet at their second shop visit. That bodes well for our service business. We're managing well through the LEAP ramp. Despite the leap growth, we're maintaining 20%-plus margins through the launch. Our military portfolio is broad and we see opportunities for growth with our next-gen technologies both in the U.S. and internationally. We were encouraged by the strong first quarter performance, especially in services.

And finally, across the whole business, we're leveraging the strength of Additive, which is a game-changer for high-tech component manufacturing. Additive is allowing us to reset our supply chain cost entitlement and we're seeing proof points across parts, systems and products. Aviation is a premier asset with over $200 billion in backlog and good visibility to long-term growth. We want to continue to invest and grow this franchise.

Next is Power. While our results here have been unacceptable, this is a fundamentally strong franchise with leading technology, a valuable installed base and expansive global reach. GE generates about 1/3 of the world's electricity and has about 1,600 gigawatts of installed capacity. Gas, which is our largest segment, remains a key part of the world's long-term power generation mix. GE has approximately 7,000 gas turbines in our installed base and we have a 20-year plus track record that demonstrates we can improve output, reliability and performance of those assets when we service them. We are a big player in grid, equipping 90% of transmission utilities worldwide. There are certainly macro and secular challenges to this business, but we are taking actions to remediate the issues that we saw in 2017 and to right-size our cost structure for a lower heavy-duty gas turbine market in the near term. This is a turnaround story, and we are confident in our ability to improve the future operating performance. We have a well-thought-out and detailed plan to reach the 10%-plus margins outlined at EPG. Overall, this is valuable franchise that will be run better moving forward.

Our Renewables business is an important part of the energy mix. 67% of 2017 global power capacity additions were from renewable sources, with some sources estimating 70% of 2018 to 2021 additions from renewable sources. We are a leading player in onshore wind, gaining market share in 2017. We are making inroads into offshore wind and have a strong hydro business. Renewables is a competitive and evolving industry but one, we think, we're positioned well in going forward.

Aviation, Power and Renewables are businesses that we feel are best positioned together to deliver results and drive shareholder value. These are all businesses marked by deep and complementary technology investment and differentiation and using that investment to grow our installed base and build high-value service stream annuities. Whether generating electricity on land or thrust in propulsion in the skies, the machines from these segments share a common core set of technologies, service platforms and global markets that make them stronger together than they would be if innovated in isolation. In fact, the first U.S. jet engine created by GE evolved from the industrial gas turbine. While one is for power and one for flight, they both share a common architecture and operating environment that allow them to naturally have a common set of technology needs.

Wind turbines, too, share many common traits. They are large spinning machines that generate megawatts of torque and power. That's very familiar to GE. I'll give you 2 examples of technology synergies. First, edge controls. For decades, we've developed industrial controls for gas turbines, jet engines and more recently, wind turbines to ensure each operates safely and at the highest levels of performance and efficiency possible. With the exponential growth of computing power in the past decade, we're now combining controls with digital technologies in a very powerful way to further optimize the way we operate and maintain these machines. At our global research center, we developed a common industrial operating system called [Edge OS], which works in a wind turbine, jet engine or gas turbine.

A second example is material science. The LEAP engine was the first to have a revolutionary new material called ceramic matrix composites, or CMCs. It's a lightweight ceramic material engineered to be as strong as metal but able to withstand much hotter temperatures. It has been a real difference maker in our LEAP product offering. The development of CMCs actually started as a project in our gas turbine business. In fact, it was because the material performed so well in the field testing with gas turbines that led us to discover it could work in jet engines as well. With polymer matrix composites, or PMCs, GE Aviation first introduced lightweight composite fan blades in the GE90 engine, and we took that knowledge and quickly adapted it for Renewable Energy's wind blades.

On the services side, we had a massive installed base across all 3 businesses with 65,000 aircraft engines, 7,000 gas turbines and 35,000 wind turbines. These products all have long lives and our services business model provides a very profitable recurring revenue stream. We realized many common synergies around how to execute and manage these long-term service contracts. The markets are similar, they're global and this is where we can tap into GE's deep global network and experience.

Digital and Additive are substantial opportunities across all 3 segments that provide benefits to enhance growth and lower cost.

We are certain that with focus and a strong balance sheet, GE will be a technology-driven growth story again in the coming years.

As I said before, we've been methodically reviewing the portfolio and looking at the best structure or structures to maximize value and position our businesses for success. We are excited about the future of GE Transportation, Baker Hughes GE and GE Healthcare.

We announced the merger of Wabtec and GE Transportation last month. We are contributing Transportation at an attractive multiple and realizing $2.9 billion of cash proceeds, while our shareholders will benefit from the compelling long-term prospects and synergies of the combined platform. The industrial logic of this deal is strong and there are good growth opportunities with GE's installed base and services offering combining with Wabtec's portfolio.

We are beginning the process of separating Healthcare immediately and expect to complete it in the next 12 to 18 months. We plan to monetize approximately 20%. We expect it to have a capital structure and capital allocation aligned to its peers. As part of the transaction, we will transfer approximately $18 billion of debt and pension obligations to Healthcare. With respect to the impact this will have on future dividends, it's our intention to maintain the current $0.48 dividend until the time Healthcare is established as a stand-alone entity. At that time, both GE and GE Healthcare will determine their future dividends with an intended payout ratio in line with their respective industry peers. Given the typically lower payout ratios in the health care industry, this will likely lead to a reduction in the aggregate GE dividend at that time.

We like the BHGE combination. Customer reception has been positive and we're gaining traction across product lines. The realization of synergies, both top and bottom line, was premised upon GE's sharing of significant technology and expertise with BHGE. This was contracted for at the time of the merger and is going well. BHGE is well positioned to thrive as an independent company. As I said earlier, we expect to substantially exit our direct ownership of this business within 2 to 3 years.

Running the businesses as the center of gravity is the third major point of our announcement today. We're implementing a new way to run the company. We will focus all of our activity in the company around our businesses with a much smaller corporate headquarters. Corporate will focus on strategy, capital allocation, talent and governance, and we will reduce the size of corporate significantly with at least $500 million of additional corporate cost-out by 2020. As we apply the same principle to our businesses, we expect incremental cost savings in the businesses during this period of time.

As you know, we have historically run several organizations centrally. This will change. Centrally run activities in shared services will be placed back in the hands of the businesses. Our business leaders will have full accountability for and ownership of their operations, and everything we do will be subject to a market test. There will be no central residual cost. Global research will now align under David Joyce. Our Global Growth Organization will be significantly smaller and focused on government relations and developing markets where we need strong resources to play its scale and manage risk. And GE Ventures will be refocused. It'll be focused on only the most urgent markets and new technologies as determined and paid for by our business leaders. Our digital strategy continues to focus on our core industries in our installed base, and we expect no cost drag from digital by 2020. We believe these actions will result in better execution, increased speed and additional cost reductions of at least $500 million. This is incremental to the more than $2 billion of cost-out we're actioning in 2018.

Now that I've walked you through our strategic review and go-forward plans, I'll hand it over to Jamie.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Thanks, John. I'll talk you through the second major point John highlighted at the outset, strengthening the balance sheet. We are very focused on strengthening our balance sheet and taking clear action to put ourselves on stronger footing. This page has our planned actions to achieve our financial policy goals over the next 2 years.

Our financial policy continues to target a net debt-to-EBITDA ratio of less than 2.5x, and we remain committed to having a strong A rating and a Tier 1 short-term rating. We plan to run the company with a higher cash balance, targeting more than $15 billion of cash on the balance sheet.

With respect to the dividend, as John mentioned, it is our intention to maintain the dividend until the Healthcare separation. First, I'll start with our leverage ratios. You should note that when we discuss net debt-to-EBITDA, we calculate the ratio along the lines of rating agency methodologies. We have included a footnote at the bottom of the page with the calculation of net debt as a reference.

As you can see, our expected net debt-to-EBITDA at the end of 2018 is approximately 3.5x on a about $50 billion of net debt. Year-to-date, higher interest rates have reduced our pension deficit by about $5 billion, which is included in our estimate of these ratios. For 2020, we expect to be at less than 2.5x net debt-to-EBITDA. This equates to about a $25 billion reduction in net debt. To achieve this reduction, we will transfer approximately $18 billion of debt and pension obligations to Healthcare with their separation, and pay down approximately $9 billion of debt in commercial paper in 2019 and 2020.

As a frame of reference, if you take 2018 numbers, EBITDA is impacted by lost Healthcare and disposition earnings, which are mostly offset by corporate cost reductions, lower restructuring and segment earnings growth over the next 2 years. This is the EBITDA of the new GE and share owners will also own Healthcare and Wabtec. We have a number of actions to take over the next 2 years, but we have a clear path to achieving less than 2.5x net debt-to-EBITDA by 2020. In addition to the transfer of obligations to Healthcare, we have multiple potential sources of cash to achieve our objective. They're listed here. Cash proceeds from our planned $20 billion of dispositions, monetization of approximately 20% of our Healthcare shares as part of the separation, the value of our Baker Hughes GE holdings and remaining 9.9% Wabtec shares and industrial free cash flow in excess of our dividend. All in, these potential transfers or sources total more than $60 billion. We believe we have ample means to bring our leverage down and achieve our net debt reduction.

Our strategy with respect to GE Capital is clear, we intend to materially shrink the balance sheet of GE Capital. We will look to sell $25 billion in energy and industrial finance assets by 2020, and our current thinking is that we will contribute $3 billion to GE Capital in 2019. We are continuing to evaluate this number, and we'll report back to you later in the year to firm this up. This planned contribution, in addition to the asset sales, allows us to achieve our targeted capital level sooner than our previous plan. We are also actively exploring options to reduce our insurance exposure. A strong balance sheet is a top priority for us, and we believe we have more than adequate resources at our disposal.

From a cash perspective, we have taken a number of actions to strengthen GE's liquidity profile and reduce our reliance on the short-term markets. We have an intra-quarter commercial paper program that we use today to fund working capital needs. During the second half of 2018, our average commercial paper balance is expected to be $10 billion, down from $16 billion in 2017. And peak usage is expected to be $13 billion, down from $20 billion in 2017. By 2020, we expect average usage to be less than $5 billion and peak usage to be about $5 billion. We are managing the business to improve their cash operations and management. We expect to have more than $15 billion of cash on the balance sheet at the end of 2018. We have also restructured our existing credit facilities. These now include approximately $40 billion of undrawn facilities consisting of a new $20 billion credit facility as well as a total of $7 billion of bilateral 1- to 2-year revolvers and $13 billion of available syndicated backup line.

One last point on the financials. John discussed the actions we're taking at corporate, which should result in additional cost reductions of at least $500 million. We are targeting a payback of less than 2 years and estimate that restructuring cost will be between $800 million and $1.2 billion. The impact to cash in 2018 will be relatively immaterial. As we action our plans, we will bring a more refined view back to you. Also, in the second quarter, we expect a $200 million to $300 million tax charge related to the decision to separate Healthcare.

The actions we are taking strengthen the balance sheet and create a stronger GE. We will reduce industrial leverage to less than 2.5x net debt-to-EBITDA by 2020 and materially shrink GE capital and improve its balance sheet. We have multiple potential sources of cash to achieve these objectives and to position the company for growth going forward.

With that, I'll hand it over to Kieran to cover GE Healthcare.

Kieran P. Murphy - *GE Healthcare Limited - Former President & CEO of Life Sciences*

Thank you, Jamie. The Healthcare leadership team is excited by the prospect of being a stand-alone company under the GE brand. I want to briefly introduce the business and explain why we have the opportunity to grow whilst improving patient outcomes, increasing customer productivity and creating better access to advanced care around the world.

This is a business with scale. We lead the industry with revenues of close to $20 billion and we're market leaders in the segments in which we play. We have the largest installed base of imaging and ultrasound equipment in the world. Our $5 billion service business and our digital presence in imaging and monitoring ensures that we have long-lasting relationships with our customers.

Our Life Sciences business is established as a leader in bioprocessing and contrast agents. These are well-established brands, which provide consistent revenue and great cash flow.

In the case of our bioprocessing business, we are designed into all of the top 10 best-selling biopharma products. And we continue to build complete system offerings in an industry with strong growth prospects for the foreseeable future.

Our operating margin profile is strong, and we see opportunities to further improve as we embark on our new journey here. We have unique position in the industry. We are the only company positioned to work at the center of an ecosystem delivering on the promise of precision health. More precise diagnosis, precise therapy and new innovative ways of monitoring patients are the means by which costs in the industry can be better controlled and outcomes improve for patients. These things are key concerns for governments and health care systems across the world.

Through the use of AI and machine learning, we see a future where the combination of in vivo and in vitro diagnostic data sets can provide new insights on the underlying causes of disease. Since we're the biggest generators of in vivo data in the world, we're starting this journey from a position of strength. In imaging, we co-invest with our customers in these exciting new areas and we've demonstrated already that we can improve workflows for radiologists and provide clinical decision support tools for doctors. For example, our imaging software can adapt automatically to users' preferences, speeding up their work. And our venue ultrasound product helps caregivers by automatically calculating cardiac output, a vital parameter in deciding the best course of action for a patient in shock.

The new paradigm of therapy will derive from better targeted clinical studies and new delivery mechanisms aimed at personalizing medicine. Through our experience in bioprocessing and cell therapy, we play a key role in industrializing the science behind this exciting and fast emerging field. For example, our KUBio line of prefabricated biomanufacturing facilities dramatically reduces the customers time to manufacturing, accelerating their time-to-market and reducing their investment risk.

Lastly, our customers can only survive in the future by ensuring greater productivity in their health systems. We see monitoring of patients and workflows as being the critical factor in safely shortening hospital stays. With our unique position in digital systems, most notably our new command center technology, we can be the exemplar in productivity and patient safety. Precision health is the future, and we are uniquely positioned to improve the care and well-being of patients.

In terms of our operating approach, we know that our future depends on delivering great outcomes for our customers. We have increased our investment in key technology areas, in partnership with our customers and emerging technology players so that we can deliver relevant innovation. We are a truly global player with commercial and service teams placed in all key established and emerging markets across the world. Our emerging markets teams have delivered outstanding growth over the past 5 years, and we see the opportunity to continue to deliver in these markets.

Our supply chain is increasingly balanced across the globe, protecting us from volatility. And we continue to invest heavily in the digitization and automation of our platforms to improve efficiency. This is an area where we have been made real progress, and we see further opportunities to continue this trend through our supply chain and product design initiatives.

Lastly, we are disciplined in operating rigor and capital allocation. We have reduced our SG&A cost, and we've invested in technology. Whilst we've been prudent in our M&A approach, we have a proven track record in acquiring and integrating tuck-in acquisitions, which have built out our portfolios in areas like bioprocess and cell therapy, whilst disposing of assets that do not meet our return expectation. Our track record of results is clear: solid revenue and operating profit growth, industry-leading margins and more than 100% free cash flow conversion.

In summary, we are announcing the new direction today from a position of strength. We have a great portfolio with great technology led by talented teams who know how to run their businesses. We operate with unique global scale and industry reach, which positions us to enable the delivery of precision health. And we see additional opportunities for growth as we embark on our new journey as a stand-alone company. We expect that the availability of capital for investment in both organic and inorganic opportunities will allow us to unlock new sources of growth. The pace of growth in new digital technologies presents us with an opportunity to further build our platform as a leader in helping clinicians across the world with tools for decision support. We want to play a significant role in this emerging area, and I strongly believe that the path of independence, which starts today, allows us to move faster and invest and collaborate with a new sense of vitality. We welcome the opportunity to run an independent GE Healthcare, and we look forward to delivering for our patients, for our employees, our customers and our partners in this inspiring and fast-evolving industry. Back to you, John.

John L. Flannery - *General Electric Company - Chairman & CEO*

I want to place today's actions in the context of a series of changes we've made in the past year. We have moved with purpose and urgency as we promised at the outset. We're taking a new approach to running nearly every aspect of the company. This includes the leadership of the company, where we've made major changes in senior management, senior management at Power and at our board. We are focused on repositioning Power and continuing to de-risk GE Capital. we have moved quickly on our $20 billion of dispositions. With yesterday's announcement on Distributed Power, we are essentially complete. We have also maximized value as you can see in the Wabtec transaction. We have grounded ourselves in a renewed commitment to operating rigor, improving execution and a focus on cash generation. We have and are continuing to cut costs aggressively. We are ahead of our plan. We've revamped our compensation programs and committed ourselves to a culture of candor, transparency and accountability. We've taken a new approach to running the company, sharply reducing corporate and positioning our businesses as the center of gravity. I'm confident that today's actions, in conjunction with other changes we've already made, will produce improved operating results going forward.

As I stand here today looking back 1 year as CEO and over the arc of GE's history, I'm excited by what I see. In short, we now have a set of premium businesses placed in the right environments to flourish in the future. That has always been our objective. We have changed many things, but the essence of GE endures. The core of the company will continue to be technology and innovation that changes the world. As I look at GE today, I see what I've always seen in my 31 years at the company, I see incredibly dedicated colleagues leading everything on the field every day. This team has fought through the past 12 months with superhuman resolve and determination, and with intense pride in the company, operating with unyielding integrity, breaking barriers with technology and innovation. We are motivated, first and foremost, by making a positive difference in the world. 8 billion people expect that from GE. 8 billion people rely on that from GE.

In the past year, I've been struck by how many customers and investors are rooting for GE. We set forth today with renewed optimism in the future of GE's Aviation, Power and Renewables businesses, we are on a path of rejuvenation and growth. We are also confident that with Transportation, Healthcare and BHGE, we are unleashing other new GEs imbued with the spirit and heritage of the company we love and respect. Our focus going forward will be on unrelenting execution to deliver the kind of performance you have expected, and should expect, from the General Electric Company.

We'll now be happy to take your questions.

Matthew G. Cribbins - *General Electric Company - VP of Investor Communications*

Thanks, John. With that, let's open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Steve Tusa with JPMorgan.

Charles Stephen Tusa - *JP Morgan Chase & Co, Research Division - MD*

Congratulations on a pretty bold move, and appropriately kind of deliberating on all this. So congrats on all the hard work. Just on the cash walk, Jamie, maybe, seems like quite a bit of resources that you have but maybe the debt is not going down as much on a headline business. Can you maybe help us walk through what is exactly included in that kind of $25 billion at year-end 2020? And I guess, there is a -- the mechanics of a commercial paper are always kind of tough for us to understand, so is there -- are we assuming that a lot of this cash is just going to eat into the commercial paper? Because it would seem that you have kind of more resources coming in, in cash than you just don't have a ton of pro forma debt reduction, if you will, right? $43 billion of kind of consolidated net debt, if you include Healthcare and add it to the $25 billion at the end of 2020, but a ton of resources coming in, like you said the $60 billion or whatever. So maybe if you can just walk us through what's included already in 2018 and then kind of how you get down to that $25 billion, where the other cash is going.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Sure. Let me -- I'll step through the net debt reduction piece first, then I'll come back and touch on the commercial paper piece. So with respect to the net debt-to-EBITDA reduction piece, really targeting the financial policy to be less than 2.5x. Again, these are rough numbers and as you mentioned, we've got ample sources or potential transfers in terms of how we get there. But really the walk is 2 main pieces. The first is we plan to transfer debt and pre-tax pension deficit over to Healthcare as they transition out. The second piece is about $9 billion of planned debt and pension paydown in the parent over the next couple of years. So those are the pieces there in terms of the roughly $25 billion reduction of the net debt. At the end of the day, the GE Industrial debt balance really would move from at the end of the first quarter about $34.5 billion to the end of 2020 at about $21 billion. And then the pension deficit has a similar walk there too, from $34 billion down to about $15 billion, I'm happy to take you through any of those pieces of it. In terms of the commercial paper piece of it, CP levels do come down significantly over the next 2 years. Now part of this, as you've referenced, is holding a higher cash balance but actually, a bigger part of it is really changes in how we're operationally managing cash. We've started a process this year of really going after both consolidating fragmented cash, decreasing cash in restricted countries. We've seen significant improvements already as we've done that; and you've seen that in some of these numbers on how they've come down. But the other piece of this is really improving the linearity of cash flows in our businesses around how we do billings and collections, how milestone payments come in and the timing of those. And we've changed our incentive structure to align to how these improvements should roll in. So that's really those 2 pieces.

Charles Stephen Tusa - *JP Morgan Chase & Co, Research Division - MD*

And did you say that -- I didn't quite capture what you said about the EBITDA, but you're going to basically offset lost EBITDA from Healthcare with cost saves. That seems like a pretty big chunk of EBITDA to offset. What is kind of the run rate of RemainCo EBITDA when all is said and done?

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

So I can walk you through that, too. So first, we'll take you through all this in our fall outlook meeting, and we'll give you our financial outlook then. But just to walk through maybe some of the rough math on the EBITDA piece, it does walk back to just below where we were in '18. And you start with 2018 EBITDA, you have to back out Healthcare and the dispositions. As you know, the $20 billion of dispositions is about $1.5 billion of EBITDA. You add back corporate cost reductions and, as you know, we'll see some of that -- a big chunk of it in '18, but John also talked about the incremental $500 million. And then you have to add back restructuring, too. And we've got a very heavy run rate of that right now. That will come down significantly over the next couple of years. And then you also have your segment earnings growth. And remember that Power, we expect improvement over the next 2 to 3 years. Aviation is coming down on their investment cycle. And so all of that really mostly offsets the losses that you see.

John L. Flannery - *General Electric Company - Chairman & CEO*

Steve, the one other thing I'd just add on sort of the overall thought around the balance sheet is a key part of today's announcement is having a strong balance sheet at the company level is a top priority for this whole transformation that we're walking through here. That's how we continue to invest and grow and make sure the businesses have the resources to pursue their organic and inorganic strategy. That was a key principle of the whole analysis that we did. And I'd say, as we look at the end state here, all entities well-capitalized, the core GE with a strong balance sheet and same with Healthcare and Baker Hughes GE. And with respect to the $60 billion that's in the deck here, I'd say that's obviously a range of options. I think the key point is we continue to have ample resources and ample alternatives to continue to de-lever and de-risk the company on top of the $25 billion. So the balance sheet's a key part of our message today.

Operator

Our next question is from Andrew Kaplowitz with Citigroup.

Andrew Alec Kaplowitz - *Citigroup Inc, Research Division - MD and U.S. Industrial Sector Head*

John or Jamie, earlier this year, you had talked about selling $15 billion of assets in GE Capital, now you're talking about selling $25 billion and also funding the GE Capital by $3 billion from the parent. Can you talk about what's changed in your thinking? Is this really just being more aggressive to get sort of the debt down and streamline GE Capital? Do we have to worry that the asset sales haven't gone as you planned or that liabilities could be worst than you expect or is this just really just getting a smaller, leaner GE, including GE Capital?

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Sure. So Andy, this is really all about materially shrinking GE Capital and actually, just to address one part of your question first. The asset sales are progressing actually quite well. We're seeing strong interest in the assets from a wide variety of sources. Price discovery seems to be reasonably in line with what we expected, so that's part is good. But really when you look at the totality of this, incremental asset sales and an incremental $3 billion in GE Capital, it really helps us achieve the targeted capital levels at GE Capital faster. And it addresses potential earnings movements we may see from asset sales, other GE Capital earnings movements and the ultimate resolution of WMC. I mentioned at the first quarter earnings call that we were evaluating some incremental asset sales. Just for more context, we've been looking at GE Capital's capitalization over the last 3 to 4 months. And in connection with this broader announcement, we just wanted to tell you our current thinking on it. So it's modeled at $3 billion. It's a moving target, we've got a lot going on with portfolio actions there, but this is what's in our internal model and this is what we've shared with the rating agencies. And we continue to evaluate not just the items I mentioned earlier, but insurance and other options around restructuring GE Capital. But we'll update you later this year as this is finalized in our 2019 plan.

John L. Flannery - *General Electric Company - Chairman & CEO*

And Andy, just on top of that just to get -- come up to company strategy level and our strategy with respect to GE Capital. As Jamie said, the core message here is to materially shrink the balance sheet of GE Capital. The $25 billion is a path on that. If you look at the rest -- the balance sheet is about $100 billion. About $85 billion of that's insurance and GECAS, in roughly equal amounts. I'd say with respect to insurance, as we said, we're looking at every way possible to keep grinding down that liability, looking at how we run the business day to day, how we invest in the portfolio, every option with our primary insurers. So we're actively exploring every option to eliminate or mitigate the risk that we see there. If we see a sensible path on insurance, we'd be highly motivated to do that. And as we alluded to earlier, with the $60 billion of overall sort of optionality, we've got the strength to continue to de-lever and de-risk if that opportunity presents itself. I'd say with respect to GECAS, that just remains a premium asset, a highly coveted asset. It has significant value. We're approached on that business all the time. It continues to thrive. And as Jamie said, the $3 billion really is addressing the capital levels that we need at GE Capital. So -- but the big picture strategy is continue to shrink.

Operator

Our next question is from Steven Winoker with UBS.

Steven Eric Winoker - *UBS Investment Bank, Research Division - MD & Industrials Analyst*

Congrats on persevering through this in a deliberate process.

John L. Flannery - *General Electric Company - Chairman & CEO*

Good morning Steve.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Thank you.

Steven Eric Winoker - *UBS Investment Bank, Research Division - MD & Industrials Analyst*

Just -- I guess, I better ask both questions at once then here. First, I want to make sure that a finer point on that implied go-forward EBITDA that you walked through earlier, sounds like it's about $10 billion based on the math in the deck that you put out. Could you also, I guess, one, give us a sense if that's about right? And then the implied free cash flow conversion given the strength of what Healthcare has contributed there? And maybe a little bit more discussion on, and I assume the dividend payout ratio, when you talk about industrial peers, is about 30% to 35%. And just squeezing in a last one, there's legacy liabilities. I'm just still a little unclear about what's specifically going away with Healthcare?

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Okay. So let me take the first few of those. So first, on the implied go-forward EBITDA. I would suggest to you that these are rough numbers on this page. We have ample sources to achieve our targets. And our plan has us coming in at less 2.5x net debt-to-EBITDA. So think about it that way. I don't think the backhand math gets you to where we think we'll be. With respect to free cash flow, you talked about Healthcare being 100% free cash flow conversion business and that is true. And when you walk through the same sort of walk I walked on EBITDA with free cash flow, I would say that lost free cash flow from Healthcare and dispositions is partially offset by the lower cost and the lower restructuring that we'll have. Healthcare is 100% free cash flow conversion. We will have a heavier concentration of long-cycle businesses. But over the next couple of years from a cash perspective, we do expect significant improvement at Power. And I mentioned before, Aviation on the investment cycle post the LEAP launch. The other thing to remember there, too, is that investors will also own a stand-alone Healthcare company and Wabtec, so that's another consideration. But again, on all of this, we'll update you in the fall at our investor meeting. John, do you want to talk dividend payout?

John L. Flannery - *General Electric Company - Chairman & CEO*

No, I think you covered that. Just as we said in the release, just make sure there's no confusion. We'll maintain our $0.48 dividend through the date at which Healthcare becomes a separate stand-alone company and the 2 boards will determine their dividend policies in line with peers at the time. And Steve, as we said, given the deltas between the Healthcare industry and industrial payout ratios, we expect that to result in a smaller aggregate dividend at the GE level.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Steve, one last thing, you asked about residual or legacy liabilities for the Healthcare piece of this. The plan is to split our pension plan and so pension obligations would travel to the stand-alone company. So that's a piece of it. And then there's really nothing else that we expect at this point in terms of legacy or residual. But if that shifts, we'd certainly update you on that.

Operator

The next question is from Scott Davis with Melius Research.

Scott Reed Davis - *Melius Research LLC - Founding Partner, Chairman, CEO & Research Analyst of Multi-Industry Research*

Great detail here. We appreciate it, particularly Jamie, the walk-through is really helpful. But John, I know we've all heard some chatter on long-term care but to be able to execute a plan like this, you must have some comfort level in your assumptions, otherwise, you'd be saddling the RemainCo with a pretty big open liability. I mean, give us -- can you give us a sense at least of where you stand versus the original assumptions you gave us? And what are the options? I mean, we've heard there's a few people potentially who want to take on the liability. But can you give us any color at all? I know it's hard when you're in negotiations but...

John L. Flannery - *General Electric Company - Chairman & CEO*

Listen, I'd say just if you go up a level, Scott, so GE Capital and insurance. So the core strategy is shrink, the core strategy with insurance is to examine every possible way whether that's operational, whether it's our investment portfolio, whether it's our reinsurance treaties with our primary insurers or whether it's some type of transaction to transfer risk. Everything is under active examination with the express intention to reduce or mitigate or eliminate the exposure that we have to that. The second -- so that's what we're trying to effect as a management team here. The second thing I'd say is, as we've laid out for you, we have, as part of this plan, and an integrated plan -- there's obviously a lot of moving pieces here, but the net effect is it generates a tremendous amount of resources to de-lever the company by the $25 billion but gives us surplus capital on top of that. And that, as I said, if we could find a final conclusion for this that made sense, be more than willing to use some of those resources to effect that. So I can't really go beyond that in terms of specifics, it's very much under negotiation. But I think we are very clear what our intent is.

Scott Reed Davis - *Melius Research LLC - Founding Partner, Chairman, CEO & Research Analyst of Multi-Industry Research*

John, anything on Predix? Any update there on how fast you're moving that down into the businesses or what the plan is?

John L. Flannery - *General Electric Company - Chairman & CEO*

So this is part, I'd say, Scott, of this overall notion of businesses as the center of gravity and so the businesses are responsible for their digital strategies, specifically, they leverage the San Ramon team for platform and other investments that make the most sense being shared. But my imperative to the businesses is you have to have your own digital strategy. You have to implement it. You can use central resources where you think that makes sense, but I want the businesses focused directly on the customers, on the applications, on solving customer problems. And I just felt they knew best how to leverage the San Ramon team and get the customer outcome. So that is included in the notion of center of gravity. That results -- and we have been going throughout the year in a reduction in the investment and spending levels or transfer some of the spending levels to the businesses. And as we said, we expect no net drag from the digital spend by 2020. And that, as you know, has been a significant negative number recently.

Operator

The next question is from Jeff Sprague from Vertical Research.

Jeffrey Todd Sprague - *Vertical Research Partners, LLC - Founder and Managing Partner*

I wonder if we could just focus on Healthcare then stand-alone a little bit since you've covered a lot of the broader GE topics. John, you mentioned a capital structure in line with peers, but if we're including pension, I guess we're coming out of the gates here about 4x levered on EBITDA. So maybe a little bit of color on how you see that moving forward? And also just interested in what the Healthcare profile might look like once you're allocating corporate and pension expense and interest expense to the RemainCo, what the EBITDA profile and maybe the key profile that business might look like?

John L. Flannery - *General Electric Company - Chairman & CEO*

Let me have Jamie just get to some of the financials, then I'll let Kieran just give you some thoughts about the Healthcare business and then I'll wrap up if there's anything needed on that.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

Okay, so first on the target capital structure. We're targeting a capital structure in line with Healthcare industry peers. You've got a wide range of peers out there between imaging and diagnostics over to Life Sciences and I think one thing to remember is that we've got a mix of both of those in our Healthcare business. Those peers are investment-grade credit. I talked before about the plan to transfer both debt and pension obligations to the Healthcare business. It's really too early to comment beyond any of that. And as this plan becomes more firm, we'll certainly get back to you later in the year with the specifics on that. With respect to sort of the Healthcare cost structure dis-synergies, maybe some of those things. Maybe just to address that for a minute before Kieran comments on the Healthcare business. In the grand scheme of things, I mean, you can think about the infrastructure in relation to the capital structure that you might pro forma. From a dis-synergy perspective, we don't really expect significant cost in the grand scheme of things. We do expect incremental cost at separation to stand up a separate public company, some IT system investment. But as you know, we've separated and moved a number of companies over the years here at GE and so it's something we're comfortable doing, we see line of sight to how we do, and it does have cost but not huge. And just again, more info as we progress with the process.

Kieran P. Murphy - *GE Healthcare Limited - Former President & CEO of Life Sciences*

So -- thanks. Look, I would just say that historically, this has been a strong cash-generating business with a good growth profile and we feel we're well positioned for the future here. So we're entering the space with great confidence.

John L. Flannery - *General Electric Company - Chairman & CEO*

Yes, I agree. And better management I would say. So -- one of the things I'd say, just to maybe take it up a level, but I think it's important to share with everyone: is that if you talk about and thought of what stays inside the company or what goes outside of the company in the overall announcement today, this is really the culmination of 10 years of observation I've had in the company, about living outside of the U.S., watching the pros and cons of delegation, going through watching how we're allocating capital, running the Healthcare business and thinking, at times, there are certain other things we might do or could pursue in a different framework. So it's a dramatic sweeping change, and we truly started this whole process just looking at what is the environment and conditions that allow the businesses to flourish in the future. That has to be the essence of our work and our efforts. And I'd say what we're announcing today is really a comprehensive process coming to its conclusion. And I looked very carefully at the portfolio, where businesses would be best positioned inside or outside of the company. And for some, Transportation, Healthcare, BHGE, we thought, by far, the best environment for value creation for the shareholders was outside of the company. And for Aviation, Power and Renewables, we thought inside the company. And again, strong balance sheet at all levels was important. So at the end of all this process, I can say that as a shareholder and with my compensation almost exclusively tied to the performance of the shares going forward, I am very excited about the package that we have here and I'm looking forward to Kieran's run with Healthcare and our Wabtec future, and we know that Baker Hughes is a really strong company with a great future. And GE will be capitalized well in strength there. So that process is important just to put the Healthcare in perspective, I think.

Operator

The next question is from Nigel Coe with Wolfe Research.

Nigel Edward Coe - *Wolfe Research, LLC - MD & Senior Research Analyst*

Covered a lot of ground, obviously, already. Just a couple more things. Just thinking on the 2, 3-year time horizon for GE Baker Hughes, I mean, that seems a bit more fungible and doable in a 1-year time frame. So just the thinking on that. And then maybe just a final crack at the EBITDA walk. It seems that you're forecasting underlying EBITDA expansion for RemainCo of about $2 billion. Jamie, is that (inaudible)?

John L. Flannery - *General Electric Company - Chairman & CEO*

Let me do the Baker Hughes part of that first, Nigel. Obviously, Baker is already a public company but beyond that, I'd say like Healthcare, there's a lot of options that we have to go from here. We'll be determining that, as we said, over the next 2 to 3 years. I think the big message here for our owners is Baker Hughes is a strong, improving asset. We had an upstream business, we made a strategic decision to combine it with a downstream business. That's been very well received by customers, a full stream offering. Lorenzo and the team is doing a very strong job integrating the businesses. We're really right in the middle of executing the merger and making sure we realize all the benefits that both parties foresaw at the time of the merger. So make sure we're getting the synergies, make sure we're getting the tech transfer, sharing best practices and know-how or going back and forth, making sure digital is permeating the business. And so I'd say that process is going very well but we want to let that process run its course. Our core objective is maximizing the value of BHGE and therefore, in turn, for GE. So when that process is completed, BHGE is going to be a very strong robust stand-alone company. We like the company a lot but in the grand scheme of our, again, portfolio analysis, we did not think it made as much sense for us to own that directly over time as to have it outside of the GE construct, if you will. So we thought the best future for that company was a pure play stand-alone. And again, the team has done a great job executing that. We want to make sure we get the full upside of that before we move from here.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

And Nigel, on your other question on EBITDA, a couple of things. So first, I'm not going to comment today on future segment earnings. We'll take you through all that at our fall investor outlook. But just to walk you back through, as we walked through the walk before, all of those things, the reduction in EBITDA for Healthcare and dispositions really offset by corporate lower restructuring and segment earnings, really mostly offset as you do that walk. So it's probably the easiest way to think about it.

Operator

The next question is from Andrew Obin with Bank of America Merrill Lynch.

Andrew Burris Obin - *BofA Merrill Lynch, Research Division - MD*

I'm going to pull a Winoker, so I'll ask a double question. So first, just to get to the math on cash, I know Steve asked it, but I'm still not clear how net debt goes down by $25 billion if we're raising over $60 billion. And the second question, are you guys all set on the structure of the Healthcare deal? Or there was some news in the press that potentially some strategics still looking at it, or are there still alternatives as to how we monetize that asset?

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

So when we talked about the $25 billion net debt reduction, that's what we're focused on, is really reducing our balance sheet by $25 billion. I talked before about the $18 billion transfer to Healthcare, the $9 billion of debt and pension paydown. When we talk about $60 billion, these are potential uses or -- sorry, potential transfers or sources of cash. So they may or may not all be used, but the potential there, we wanted to really show you how we're thinking about where we could go to effect these changes.

John L. Flannery - *General Electric Company - Chairman & CEO*

And then on Healthcare, I'd say the 80-20 is a marker right now for the path we could go down. We're going to look at all the options, obviously, about the sequencing, timing, spins, splits and we're going to do that in the most effective way possible. But I think the core message for investors is it's a source of financial resource to the parent company and our investors are going to end up owning directly a stand-alone well-capitalized company. So the mechanics of this I think could move around a little bit as we optimize that in 12 to 18 months. But the big picture is stand-alone separate company and some financial resources to the parent.

Operator

The next question is from Julian Mitchell with Barclays.

Julian C.H. Mitchell - *Barclays Bank PLC, Research Division - Research Analyst*

So just a question around the free cash flow profile of the RemainCo. I just wondered if on the Power side, you've obviously set your expectations for EBIT margins. Maybe just give us a sense of how you think about free cash conversion to Power through the cycle, or putting it another way, you've got the 10% plus EBIT margin goal, what sort of free cash flow margins should that correlate to? And then a longer-term one on that same point on free cash flow. If you look at GE historically, you had a lot of short-cycle free cash flow to fund the periodic belts of the CapEx or R&D in engines and gas turbines. That short-cycle aspect has largely been divested. So how comfortable do you feel about the free cash flow cyclicality or volatility in terms of the RemainCo?

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

So with respect to both of those, I walked you through before our view on free cash flow, that today we are targeting 90% free cash flow conversion for '18 and into '19, until the time of the Healthcare separation. When you break that down post the Healthcare separation, I think you're spot on, that we'll have a heavier concentration of long-cycle businesses. With respect to Power, given the market softness that we have, we do expect to continue to feel pressure in Power fee cash flow conversion over the next couple of years. With respect to Aviation, we've got healthy free cash flow conversion there, and that continues to improve as we get into the next couple of years in '20 and '21 as they come down their investment cycle and as they continue to prove -- improve their position. I think the other thing you have to couple with this is, I think you're right, we are shifting the profile of the company, short cycle, long cycle, but we're also really taking significant steps to strengthen the balance sheet and be in a different position in 2 years. So as we look at the total mix here, we feel good about the positioning of the company and how that'll affect the free cash flow conversion and things going forward.

John L. Flannery - *General Electric Company - Chairman & CEO*

And Julian, I may just add a comment on Power. We're obviously going through a deep turnaround right now. But our overall strategy, as we look forward 2 years, 5 years, 20 years, the industry is not going away. Gas stays in the mix. I mean, the big picture is Renewables are up. Coal, nuclear, down. Gas remains an important part of the global energy mix. There's quite an interesting report out from Bloomberg last week, the electricity produced from gas forecast to increase by 20% by 2050. So we're a leader in that business. We're playing a long-term game there. It's going to be choppy in the next 1 to 2 years as we go through with this but it's a valuable asset. And I have a lot of confidence in Russell and the team to execute the plan we have. So we've got to keep a long-term perspective, I think, on the power industry and our position in it; and then to the challenges we're working through right now.

Operator

And our final question is from Christopher Glynn with Oppenheimer.

Christopher D. Glynn - *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Most of the questions have been asked. Just curious on the long-term care insurance, it sounds like one of your options might be using the extra liquidity, just to pay the whole thing down prematurely relative to the original plan. Is that a proper read?

John L. Flannery - *General Electric Company - Chairman & CEO*

No. I'd say this is obviously a long-term liability that unfolds over time. So it's not the same concept, if you will, of saying retiring a fixed amount of debt. So continue to look at ways to manage that liability down as aggressively as we can, but it's not as straightforward as paying off a loan.

Jamie S. Miller - *General Electric Company - Senior VP & CFO*

And I would say, as John talked about before, our focus with GE Capital is to materially shrink the balance sheet and there's multiple ways that we are looking at and/or plan to effect that. So we're evaluating options and as John talked about, we've got ample resources as we work our way through that.

Matthew G. Cribbins - *General Electric Company - VP of Investor Communications*

All right. I'd like to thank everyone for joining today, and just to remind you a replay of today's call will be available this afternoon on our investor website. And then we'll be back to you on the second quarter earnings call on Friday, July 20. John?

John L. Flannery - *General Electric Company - Chairman & CEO*

Great, Matt. Thanks. I'll just say in conclusion, from day 1 as CEO, we have promised you a deep and thorough and thoughtful analysis of the company and the management of the company's assets and future direction for the company. And this really is a culmination of that review. This is our path forward, this is our plan. We're finished with that phase. I call this the end of the beginning. We're now focused extremely on executing on the plan. And again, I think as we summarized, we've focused the portfolio to make sure it can grow and create the most shareholder value, that's been our top priority; balance sheet strength, central to the story; running the company with the businesses as the center of gravity, we didn't talk much about that but this is a massive change in the sort of software inside the company that I think is important and will deliver results. And when it's complete, we'll have a core GE Company, premier high-tech industrial company, strengthen the businesses outside of the GE portfolio, and I'm excited to work on the plan, and it's a privilege to lead the company. And we're looking forward to updating you as we go. So thanks for your time.

Matthew G. Cribbins - *General Electric Company - VP of Investor Communications*

Thank you.

Operator

Thank you. This concludes your conference call. Thank you for your participation today. You may now disconnect.
