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GE's Jeffrey Immelt: All Boxed In

No matter what the CEO does to try to save his company, it has lost its aura of greatness

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Immelt wants to shift GE's focus to infrastructure, media, and health care
Michael Gillette

On the day before President Barack Obama's inauguration, Jeffrey R. Immelt tried to give [General Electric \(GE\)](#) investors his own brand of hope. With the world going through a fundamental reset, the GE chairman and CEO told MSNBC viewers: "We've got to come out of this a brand-new company."

That vision has since gotten lost amid the day-to-day concerns that have come to haunt GE. In recent months Immelt has been buffeted by complaints over the company's struggling GE Capital unit and by slowing growth in some of its industrial operations, leaving him with little choice but to play defense. Instead of rolling out radical new solutions to GE's problems, Immelt has been bogged down in dealing with finance issues. Instead of announcing bold new acquisitions, he has cut the dividend to help preserve cash. Instead of selling off underperforming units to strengthen operations, Immelt has had to hold on to things he doesn't want.

In short, Immelt has a long way to go before he creates a brand-new GE.

The question is what Immelt, 53, can do from here. With the expectations of shareholders and analysts now so low, this would seem like the perfect opportunity for the embattled CEO to reshape the conglomerate for the future. If any company can fight its way back to greatness, surely it's GE, which booked \$18 billion in profits last year and is sitting on a \$48 billion cash hoard. As Sanford C. Bernstein analyst Steven Winoker says: "You want to believe that if GE is

as well-managed as it always has had the reputation for being, then now is the time that it should be taking advantage of distressed pricing on strategic assets."

HEMMED IN

But a closer look at GE's predicament reveals that Immelt's options are quite limited. While he has raised \$15 billion in fresh capital, slashed costs, and diversified GE Capital's funding in recent months, the economic climate makes it difficult for him to do much more. He's focused on building businesses in areas like [green energy](#) and infrastructure that could benefit from [stimulus money](#). That builds on a strategy forged years ago. If he wanted to take dramatic steps to transform GE's portfolio—and there are scant signs he does—he simply can't. "He's totally hemmed in," says [Boston University School of Management](#) professor N. Venkat Venkatraman.

Many CEOs staring down today's problems are asking themselves the famous questions that Peter Drucker once posed to Immelt's predecessor, Jack Welch: "If you weren't already in this business, would you enter it today?" And if the answer is no, "what are you going to do about it?" GE's current chief might have lots to offer on the first question. On the second, his choices are few.

Start with GE Capital, the finance arm with \$637 billion on its balance sheet and long-standing businesses from aircraft leasing to equipment financing. In recent years it bet big in businesses such as commercial real estate and consumer loans in Eastern Europe. As economies flail and real estate values teeter, shareholders have grown increasingly nervous about GE's exposure to losses. "I don't think investors want to sit through another cycle with GE Capital," says JPMorgan Chase ([JPM](#)) analyst C. Stephen Tusa. "They would rather own a pure global infrastructure play." Immelt wants to reduce the unit's impact. Last year he announced he would sell the \$29 billion credit-card business, which issues store-brand cards for retailers like Gap and J.C. Penney, but no buyers appeared. Although profitable in 2008, the segment faces rising delinquencies and credit costs as unemployment grows.

THE MOST DARING MOVE

When it comes to transforming his financial operations, Immelt may need to cut GE Capital substantially if he wants the stock to trade at the multiple of an industrial company, analysts say. The most daring move would be to separate the financial and industrial businesses. While that's not impossible, it's highly unlikely. Even if investors were lining up to buy all or part of GE Capital, which they're not, Immelt is unlikely to float the finance unit for several reasons. The stable industrial businesses enable GE Capital to tap its parent's still-enviable credit rating and help support the financial unit's \$466 billion in debt.

A split would require GE to inject as much as \$32 billion in additional funds to back up the obligations of GE Capital, estimates Richard Hofmann at CreditSights. It would force the finance arm to renegotiate credit lines with some 65 banks worldwide and make its borrowing costs escalate. The credit-rating agencies have given GE a AA+ rating—the second-highest of the 20 grade levels that Fitch and Standard & Poor's can award. GE Capital alone would get a rating no higher than A, forcing it to post up to \$15 billion in extra collateral and capital, Hofmann notes,

to keep borrowing costs at the current level. "It would have an exorbitant amount of cost associated with it," notes Sterne Agee analyst Nicholas P. Heymann. An independent GE Capital could potentially turn to the government for help as so many other finance companies have in recent months. But bailout fatigue in Washington means a standalone unit might not receive taxpayer support.

Instead, Immelt is committed to GE Capital even if it's likely to drag down earnings through at least 2010 and may never turbocharge them again. Still, the GE chief has reason to keep a stake in the world of finance. GE Capital's businesses could grab market share from worse-off rivals when economies improve. CFO Keith Sherin has said that GE will not need to raise external capital this year, even if economic conditions worsen, adding that the finance arm should make a profit in 2009. Despite repeated assurances from GE that its obligations are under control, though, some suspect the worst is yet to come. Although GE exited the U.S. subprime mortgage business a few years ago, it could see further dips in areas like commercial real estate or leasing as ripple effects of the recession take hold.

While Immelt tries to move away from certain financial businesses, he could look to build up the industrial side. The company's massive cash pile would make it easy to pick up some industrial gems. But the CEO needs to conserve cash to protect against losses in GE Capital. "GE industrial, which is extremely well placed globally, can't augment their position until these finance markets improve," says TIAA-CREF analyst Bob Spremulli. "They can still make small acquisitions, but if something bigger came along that was an opportunity, they would not be able to do that right now." Instead, Immelt is running the businesses as efficiently as possible, cutting \$5 billion in costs companywide while beefing up research and investing in areas such as green energy. A GE spokesman says Immelt's strategy is to make small acquisitions and grow them.

One blow: the loss of GE's prized AAA credit rating, the first downgrade in five decades. Although the rating dropped only a notch (or two, in the case of Moody's), Immelt can't afford to let it fall significantly further. Right now the ratings are stable, and the industrial businesses are expected to make enough cash to keep things that way. If GE doesn't get the \$2 billion in discretionary cash flow Standard & Poor's ([MHP](#)) expects the businesses to produce for 2009, the ratings agency says it could revisit its outlook. Any moves to use cash for acquisitions beyond small-scale targets would not be welcomed by the agencies or shareholders. Says Robert Schulz, a managing director for Standard & Poor's: "We would expect them to restrain actions on the acquisition front."

In fact, some pundits believe that what Immelt should do right now is make the entire conglomerate smaller. Analysts were debating whether GE was too big at \$107 billion a year in sales, the level when Immelt took over in 2001. Last year it rang up more than \$180 billion. Immelt has long argued that scale gives GE an advantage. But University of Western Ontario business professor Stewart Thornhill argues that "beyond a certain point, scale becomes an impediment, because it's just too big to manage effectively."

ANXIETY AMONG THE TROOPS

Immelt can't offload units—even the iconic appliance and lighting businesses didn't attract buyers when he tried to sell them last year—but he can do more restructuring. Ronald N. Ashkenas, managing partner at Stamford (Conn.) consultancy Robert H. Schaffer & Associates, thinks carving up the industrial businesses into smaller units could help GE become more entrepreneurial. "Whenever you have very large businesses," he says, "somebody's often 8 or 10 steps away from people who actually make a decision."

Given the prospect of leaner times for the foreseeable future, what might happen to GE's famous talent pool? Its long tradition of differentiating among employees and rewarding top talent with stock is tough at 10 bucks a share. Managers who came of age in a culture of success may be taking a hard look at their options. Bill Conaty, GE's former human resources chief, who retired in 2007 after 40 years with the company, says energizing staff has to be one of Immelt's key priorities. The GE chief has pledged to spend \$1 billion on leadership training this year, the same as in 2008. But he has put the long-term cash compensation plan on hold, instead granting stock options to reward and retain top performers. GE says that turnover among the executive ranks is stable. Still, Chicago-based recruiter Peter D. Crist finds GE executives in their late 30s and early 40s are more responsive to his calls these days, although "right now they're staying with the devil they know."

Immelt is clearly in what University of Michigan Ross School of Business professor Noel M. Tichy calls "the fight of his CEO life." All he can really do is control risk, cut costs, and limit investments in the businesses he'd like to shed, while keeping stronger businesses humming to generate more cash. Given the state of the market right now, that's not a bad approach. In fact, many would argue it's pretty good. But for now, GE no longer exudes the same aura of greatness.

With Mara Der Hovanesian and Dean Foust