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How Jeffrey Immelt's 'Success Theater' Masked the Rot at GE

A culture that disdained bad news
contributed to overoptimistic
forecasts and botched strategies

By Thomas Gryta, Joann S. Lublin and David Benoit

Feb. 21, 2018 11:37 a.m. ET

Jeffrey Immelt, the longtime boss at General Electric Co. GE -1.70% ▼, was a polished presenter who held court each year at a waterfront resort off Sarasota, Fla., where industrial executives and Wall Street listened for his outlook on the conglomerate.

"This is a strong, very strong company," Mr. Immelt said at the event last May.

On that Wednesday morning, though, he looked shaky to some people in attendance, running quickly through highlights of 27 slides in the ballroom of the Resort at Longboat Key Club. He defended his long-held 2018 profit goal, an optimistic benchmark Wall Street had long abandoned.

"It's not crap. It's pretty good really," he told the room, referring to GE's recent financial performance. "Today, when I think about where the stock is compared to what the company is, it's a mismatch."

It *was* a mismatch. On that day, GE shares were trading near \$28. They would go on to collapse over the next six months while the stock market set fresh records. Today, they trade below \$15.

GE's precipitous fall, following years of treading water while the overall economy grew, was exacerbated, some insiders say, by what they call "success theater." Mr. Immelt and his top deputies projected an optimism about GE's business and its future that didn't always match the reality of its operations or its markets, according to more than a dozen current and former executives, investors and people close to the company.

This culture of confidence trickled down the ranks and even affected how those gunning to succeed Mr. Immelt ran their business units, some of these people said, with consequences that included unreachable financial targets, mistimed bets on markets and sometimes poor decisions on how to deploy cash.

"The history of GE is to selectively only provide positive information," said Deutsche Bank analyst John Inch, who has a "sell" rating on the stock. "There is a credibility gap between what they say and the reality of what is to come."

Said Sandra Davis, who knows several GE executives as the founder of MDA Leadership Consulting: "GE itself has never been a culture where people can say, 'I can't.' "

Within weeks of the May meeting, Mr. Immelt announced his retirement. By year-end, GE under a new leader had cut its dividend in half and triggered a restructuring that is expected to eliminate thousands of jobs and cast off more than \$20 billion worth of assets. Today, federal regulators are examining GE's accounting for certain transactions, and new CEO John Flannery is considering breaking up the 125-year-old company.

The tumble is all the more stark for a company that embodied the managerial success of American business and its industrial power. GE once had the highest market value of any U.S. corporation. Its alumni have gone on to run companies such as Boeing and Chrysler.

Few knew just how badly ailing the American icon was. Even GE's board didn't realize the depth of problems in the biggest division, GE Power, until months after directors had replaced Mr. Immelt, according to people familiar with the matter. For the 2017 fourth quarter, GE reported lower revenue and, after a charge related to a review of its insurance business, a loss of nearly \$10 billion.

“Many of us are in some level of shock,” said a former director.

Investigations are under way inside GE, including at the board level, seeking to determine how it all happened, some of the people said.

Several GE executives were aware the 2018 profit goal of \$2 a share wasn’t realistic, they said, and some were surprised Mr. Immelt stuck to it at the May event.

“I led GE through multiple industry cycles, 9/11, recessions, and the global financial crisis. My leadership team always focused on the task at hand,” Mr. Immelt, 62 years old, said in a written statement. “Because we had a culture of debate and external competitiveness, GE built a set of industrial businesses that lead in their markets.”

At a conference hosted by Axios in November, the month after he stepped down as chairman ahead of schedule, Mr. Immelt noted that GE is “125 years old; we go through cycles,” and said he was “fully confident that this company is going to thrive in the future.”

A spokesman for the former CEO pointed to his decision to purchase \$8 million worth of GE shares in 2016 and 2017. That included 100,000 shares in mid-May at a price roughly twice today’s.

Former GE Chief Financial Officer Keith Sherin, who worked alongside Mr. Immelt during challenges such as the financial crisis, said the CEO would methodically approach a problem with his team, consider multiple viewpoints and communicate regularly with the board, making sure executives stayed focused on the most important issues. “I never found him to be overly optimistic,” said Mr. Sherin, who retired in 2016.

But Mr. Immelt didn’t like hearing bad news, said several executives who worked with him, and didn’t like delivering bad news, either. He wanted people to make their sales and financial targets and thought he could make the numbers, too, they said.

The optimism was evident in how Mr. Immelt and the board used the company’s cash. Over the past three years, GE spent more than \$29 billion on share repurchases, at an average price of almost \$30, about twice the current level. That included billions of dollars spent less than a year before GE suddenly found itself strapped for cash last fall.



Gas turbines, seen under assembly in Greenville, S.C., are a big business sector for GE but one that has struggled.
PHOTO: LUKE SHARRETT/BLOOMBERG NEWS

Mr. Immelt won applause from those who believed in him. Trian Fund

Management LP, which invested \$2.5 billion in GE in 2015, wanted it to buy back even more stock. The activist investor urged the company to borrow \$20 billion for repurchases (which it didn't do), based on a belief that the profits Mr. Immelt was promising would send the stock soaring when they arrived.

Instead, at Mr. Immelt's retirement in August the stock was below its level when he took over 16 years earlier. Including dividends, GE gained 8% with Mr. Immelt at the helm, while the S&P 500 rose 214%. Since he stepped down, the stock has lost about 43%, erasing almost \$94 billion in market value. The relationship with Trian deteriorated last year and the investor successfully pushed for a board seat to assert influence.

Mr. Immelt's successor, Mr. Flannery, was one of his lieutenants, a 30-year GE veteran. In November, Mr. Flannery slashed the 2018 financial targets his former boss had stuck with a few months earlier. Instead of \$2 a share GE now projects \$1 to \$1.07. It now expects to be at the lower end of that range. Gone now are most of Mr. Immelt's team, including his finance chief and head of the power division.

“GE’s customers, investors and employees want us to focus on the future. We are building a stronger, simpler GE,” Mr. Flannery said in a written statement. “In the last decade, the GE team built a number of excellent businesses.”

Several directors discussed in November whether the entire board should be fired, according to people familiar with the meeting. Instead, what had been an 18-person board will lose half its members but soon add three new directors in coming months.

Mr. Immelt’s predecessor, Jack Welch, delivered steady profit growth and sent shares soaring in the 1980s and ’90s by striking deals and aggressively slashing costs and jobs. Mr. Welch also built up a huge lending business called GE Capital that for years generated outsize profits—but nearly sank the company during the financial crisis on Mr. Immelt’s watch.

When GE later sold most of GE Capital, Mr. Immelt laid out a strategy in which the industrial businesses would grow enough to offset the lost cash flow from the financial unit, so that GE’s long-term financial projections and dividend were sustainable. It didn’t work out that way. Free cash flow wasn’t sufficient to cover the dividend for years.

During his tenure, Mr. Immelt ramped up research spending and hired thousands of programmers to develop software for the machinery GE makes. Results were strong at two of GE’s big units, aviation and health care (medical equipment). But sales and profits slumped at the enlarged oil and power units, creating serious problems.

Starting early in his tenure, Mr. Immelt bet heavily on the energy boom. Acquiring companies that help drillers pump and transport fuel, he had GE spend more than \$14 billion over 10 years, most of it based on higher oil prices than today’s.

He also spent more than \$10 billion to scoop up assets from a turbine rival, a transaction that closed just as that market was cooling. The deal was a 2014 agreement to acquire Alstom SA’s [ALO 1.81%](#) ▲ power business, one of GE’s biggest industrial acquisitions and a key part of Mr. Immelt’s strategy.

Mr. Flannery, then in charge of business development, favored the deal. “The power sector is core to GE’s future and it has excellent long-term growth prospects,” he said after the 2014 announcement. Now the new CEO says the price was too high.

The acquisition suffered in part because of an 18-month regulatory review in Europe. To get the deal done, GE had to make sure French jobs were secure and shed certain assets and technology.

Some GE executives were concerned the compromises changed the calculation too much. Alstom's power business suffered while the sale was in limbo, and some in the leadership at GE wondered if it should drop the deal. Mr. Immelt and power division leaders were determined to close the transaction, people familiar with the decision said.

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Defenders of the deal say it gave GE a much larger base of customers for its services and provided technology to produce a more efficient gas turbine. While the timing wasn't ideal, said one person close to the transaction, the company

couldn't control when such assets became available.

"When the EU delayed the deal, GE should have walked away," said Scott Davis, an analyst at Melius Research. "The fatal move, however, was how GE acted after the deal closed."

Rather than using his unit's greater size to raise prices, GE Power's then- CEO Steve Bolze moved to gain market share, undercutting rivals such as Siemens AG to win sales for GE's biggest gas turbines, analysts say.

At the time, Mr. Bolze was among those competing to be the next head of GE. He was bullish on the power unit's prospects in March 2017 but warned of possible volatility. "I am not naive on the market," Mr. Bolze said at an investor meeting that month, predicting a flat market for the biggest turbines. In June, days after losing out for GE's top job, Mr. Bolze said he would leave.

It wasn't until a meeting in September that the board learned the depths of the problems at the division, which accounts for 30% of GE's approximately \$122 billion in annual revenue. GE Power was sitting on too much unsold inventory and was discounting deals to hit sales projections.

Mr. Immelt's optimism was part of the problem, according to some people close to the situation. They said he told the board that management had identified risks in the power business, yet downplayed them. The probability and risk were way off, one said.



Former CEO Jeff Immelt, left, former power division chief Steve Bolze and John Flannery, now CEO, left a 2014 Paris meeting about buying competitor Alstom. PHOTO: ETIENNE LAURENT/EPA/SHUTTERSTOCK

Mr. Immelt's spokesman said the board and executive team were informed of the company performance and were involved in setting financial targets.

Orders in the power division dropped 25% in the fourth quarter of 2017 from a year earlier, and the unit's profits for the full year fell by nearly half to \$2.8 billion. In December, GE said it would cut 12,000 jobs in the power business, or nearly 18% of the division's workforce, and has replaced much of the management of the unit.

Lisa Davis, the U.S. chief of Siemens, said the German company's executives "have seen this decline coming for the last several years." So Siemens had reduced its capacity in its power business, she said, while GE bought more.

GE also had been selling upgrades to make existing gas turbines run more efficiently. As recently as July, it was telling investors it would sell as many as 165 so-called advanced gas path, or AGP, upgrades in 2017. In October, the company cut that target in half, and it said it expects to sell just 40 upgrades in 2018.