

EUREKA *report*



The AAA team

By Elizabeth Moran
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PORTFOLIO POINT: The AAA-rated bonds offer a slice of one of the world's biggest companies, and being in Australian dollars there is no currency risk.

Most investors have at some stage held a term deposit, probably without realising that it is by definition a fixed-income investment. Like bonds and other types of fixed-income investments, term deposits offer a rate of interest that varies depending on the maturity and the issuer's credit rating.

Term deposits are hard to beat for smaller investors, assuming they are prepared to lock funds away for a set period.

But for investors prepared to take on slightly more risk, with a little more capital and a longer investment horizon, there are many other options that may be suitable, as you can see below.

-Investments with small minimum amounts

Security type	Min investment amount	Access
Term deposits	\$1,000	160 ADIs
Commonwealth government bonds	\$1,000	Broker/government
Semi-government bonds	Varies QTC \$5000	Broker/government
Direct bonds#	\$50,000 face value	Specialist brokers
Retail bonds (secondary market)	No minimum	ASX
Listed hybrids (secondary market)	No minimum	ASX
Managed funds	From \$5000	Financial planners/Funds

Source: FIIG Securities

This week we review the bonds of one of the biggest companies in the world: General Electric (GE). These bonds are available to retail investors in parcels of \$50,000 from specialist brokers. Even more importantly, they are priced in Australian dollars, which eliminates currency risk.

GE has been part of our \$1 million bond portfolio (click [here](#)) since we began this column and remains one of our top picks for investors looking to build a portfolio of fixed-interest investments. With the group reporting third-quarter earnings over the weekend, now is an opportune time to discuss the company and its operations for investors looking for affordable ways to enter the bond market.

Background

During the GFC, its GE Capital Corp Division (GECC), which issues bonds on behalf of the group, incurred significant losses and the company lost its AAA rating. GE bonds issued through the subsidiary suffered with many investors expecting the group to divest the division. However, GECC played an important role helping industrial companies finance equipment purchases and during the crisis the division was granted bank status, which gave it access to a

range of supportive credit lines.

The division remains a core holding of the group and is a better proposition following its restructure. For the year to September 30 it contributed \$US630 million to profit. The GECC 2019 bond reached a low of under \$60 in March 2009 and those investors that bought at the time have made a healthy profit, with the bonds now trading close to face value of \$100.

If bought today, the returns on the GECC bonds are much lower and reflect the size, diversity of earnings, management and complementary businesses that make GE a low-risk investment and a healthy addition to any portfolio.

Description

GE is an internationally diverse conglomerate with operations that complement each other, providing ongoing opportunities for growth yet resilience in times of decline. GE began trading in 1892 and has links to Thomas Edison, inventor of the electric light globe.

Today its 300,000 employees serve clients in more than 100 countries, demonstrating a high level of product and geographical diversification. One of only a handful of highly rated US industrials, GE had a market capitalisation of \$US174 billion at last Friday's close.

In 2009, it delivered solid results despite the tough economic climate, with earnings of \$US11.2 billion and industrial cash flow from operating activities for the year remained strong at more than \$US16.6 billion.

GE has five business divisions.

1. Technology Infrastructure

Aviation produces, sells and services jet engines, turboprop and turbo shaft engines, and related replacement parts for use in military and commercial aircraft.

Enterprise Solutions offers protection and productivity solutions to some of the most pressing issues that industries face: safe facilities, plant automation, power control and sensing applications in the operating environment. This includes the full spectrum of security solutions, from card access systems to explosives and narcotics detection.

Healthcare has expertise in medical imaging and information technologies, medical diagnostics, patient monitoring systems, drug discovery and biopharmaceutical manufacturing technologies.

Transportation provides technology solutions for customers in a variety of industries including railroad, transit, mining, oil and gas, power generation and marine.

2. Energy Infrastructure

Energy serves power generation, industrial, government and other customers worldwide with products and services related to energy production, distribution and management.

Products include:

- Steam turbines and generators for the electric utility industry and to private industrial customers for cogeneration applications.
- Nuclear reactors, fuel and support services for both new and installed boiling water reactors.
- Aftermarket services, including equipment upgrades, long-term maintenance service agreements, repairs, equipment installation, monitoring and diagnostics, asset management and performance optimisation tools.

Oil & Gas supplies technology-based equipment and services for the entire oil and gas industry – from drilling and completion to production, transportation, refining, processing, petrochemicals and plastics.

3. GE Capital

Aviation Financial Services offers financial products to airlines, aircraft operators, owners, lenders, investors and

airport developers. Financial products include leases, aircraft purchasing and trading, loans, engine/spare parts financing, fleet planning and financial advisory services.

Commercial Finance focus is mid-market through loans, leases and other financial services to customers, including manufacturers, distributors and end-users for a variety of equipment and major capital assets.

GE Money is a leading provider of financial services to consumers and retailers in over 50 countries (including Harvey Norman). Products include: private-label credit cards, personal loans, bank cards, auto loans and leases, mortgages, debt consolidation, home equity loans, corporate travel and purchasing cards, deposit and other savings products, small and medium enterprise lending and credit insurance on a global basis.

4. NBC Universal

NBC Universal owns and operates a portfolio of news and entertainment networks including a motion picture company, significant television production operations, a television stations group and world-renowned theme parks. GE and Comcast have signed a definitive agreement to form a joint venture creating a new entertainment company that will be 51% owned by Comcast, 49% owned by GE, and managed by Comcast.

5. Consumer & Industrial

Consumer & Industrial sells products directed to both consumer and industrial applications. GE sells and services major home appliances including refrigerators, freezers, electric and gas ranges, cooktops, dishwashers, clothes washers and dryers, microwave ovens, room air conditioners, and residential water systems for filtration, softening and heating.

Third-quarter results

GE's total sales were \$US35.9 billion for the quarter or down 5% with the previous corresponding period but consistent with the first half of 2010. Revenues were impacted by lower equipment sales and reduced GE Capital assets.

The company reported earnings from continuing operations of \$3.2 billion, up 32% from the previous corresponding period and equipment orders increased by 9%, including 33% growth in Technology Infrastructure. Healthcare orders in China and India improved by more than 20%.

GE Capital performed as expected, generating \$US832 million in earnings from continuing operations. Losses continue to decline across the portfolio, with every segment except for commercial real estate producing a profit. At the end of the quarter, GE had \$US78 billion of consolidated cash and equivalents.

Value

With its AAA rating GECC bonds are great value at present, with a better credit rating than our much-lauded big four banks. In theory this should mean that GECC bonds trade at a lower spread, however, the current yield to maturity for GECC is significantly higher than that offered by the senior debt on offer from the big four.

Separately, the yield to maturity is only slightly less than the bank's subordinated debt which needs to compensate investors for its place further down in the capital structure. As such, I feel that this anomaly in the market means that GECC offers investors great value given the low risk involved.



*Elizabeth Moran is director of fixed income research at **FIG Securities**.*
