THE WALL STREET JOURNAL.
WSJ.com

BUSINESS | MARCH 3, 2009

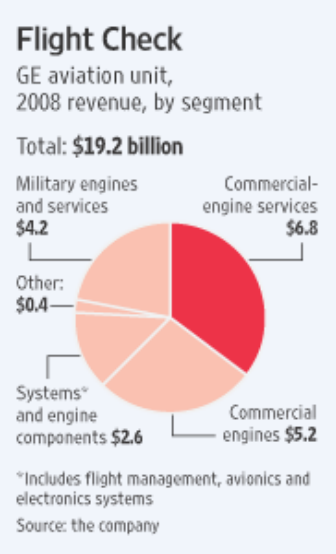
GE's Focus on Services Faces Test

As Aviation Unit Leans on Fixing Engines to Offset Weaker Sales, Rivals Step Up Their Offerings

By PAUL GLADER

EVANDALE, Ohio -- Amid the downturn, General Electric Co. is banking on making money by fixing things it has already sold. But those hopes are being tested as competitors step up their own services offerings.

From aircraft engines to locomotives, GE expects that 75% of its industrial operation's $85 billion in revenue will come from services this year, up from 65% in 2007. To support that goal, GE has been investing in new equipment and taking other steps to improve its service offerings.



The company needs all the cash it can get, with declines projected for the conglomerate's financial-services operations and its credit ratings in danger of being cut. The company last week reduced its dividend to preserve cash, and the company's shares tumbled 10% Monday.

Companies in other industries, such as Siemens AG and Caterpillar Corp., also are leaning on service revenue as product sales slow. At United Technologies Corp., whose products include Otis elevators and Sikorsky helicopters, roughly 40% of revenue came from parts and services last year. United Technologies unit Pratt & Whitney, a competitor to GE in aviation, has been looking to grab work servicing GE engines.

After-sales services and parts typically yield 25% of revenues and nearly 50% of profits for industrial companies, according to consulting firm Accenture Ltd.

At GE's aviation unit, total orders fell 12% in the fourth quarter as higher fuel costs and plunging demand drove airlines out of business. But rising service orders propelled a 21% profit increase for the unit. GE's backlog in aviation services rose 9.5% last year to $55.2 billion, representing nearly half of the company's total services backlog.

GE made military-aircraft engines from 1940 to 1970, and branched into commercial-jet engines in the 1970s to power such aircraft as the Boeing 747. GE engines can cost up to $30 million each. But GE, like other engine makers, makes little profit on an engine sale. Even in good times, the higher profit margins are on spare parts and engine repairs.

GE, based in Fairfield, Conn., is facing stepped-up competition, however. Pratt & Whitney in 2006 launched a rare assault by one engine maker on a rival's core business, with a campaign to win service contracts on an engine made by a joint venture of GE and the Snecma unit of France's Safran Groupe SA.

Kevin Michaels, a partner of AeroStrategy LLC, a consulting firm in Ann Arbor, Mich., says Pratt & Whitney has faced "a difficult road," in part because United Airlines grounded much of a Boeing fleet that would have used Pratt &

Whitney parts.

Nicole Parent, an analyst at Credit Suisse, says GE's aviation-services operation remains solid, in part because of the number of GE engines in flight. Services orders were up 9% in the fourth quarter, she says.

GE has sold $13 billion in aircraft engines since 2006. Over their 30-year life, those engines will generate about $90 billion in service revenue, GE Chairman and Chief Executive Jeffrey Immelt said at a recent presentation.

A Pratt & Whitney spokesman says the company is offering GE customers a choice and still profits from taking even bits of market share.

Independent parts makers such as Heico Corp. and Chromalloy Gas Turbine Corp. also hope to whittle away a portion of GE's business.

"The reason they want to do services is primarily to control the parts," says Eric Mendelson, president of the flight-support group at Heico in Miami. He estimates that GE accounts for $3 billion of the roughly $17 billion in annual sales for commercial-aircraft parts. His strategy isn't to take over GE's market share but to prevent a total monopoly, he says.

In 2005, GE consolidated several aviation-service businesses into one brand, called OnPoint. Last year GE transferred Tom Gentile, a customer-service and marketing specialist, from its financial-service businesses in Australia to give OnPoint its own overhaul and speed service time.

GE also brought in more-efficient equipment for its two dozen OnPoint facilities world-wide -- from Texas to Brazil to Japan -- that overhaul engines or repair damaged components. GE employs squads of mechanics who will fly anywhere in the world within 24 hours to repair a GE engine while it remains mounted on a jet's wing.

Working recently in GE services facility in this Cincinnati suburb, special-process engineer Mandeep Sahota opens an induction oven and shows off a fist-size, freshly braised, nickel-alloy blade: a small piece inside the engine for a Boeing 737. Mr. Sahota, 28 years old, points out racks of worn blades, awaiting their turn in the oven. The $250,000 machine, installed in September, can repair a blade in two hours, instead of five. "It's a microwave instead of an oven," says Chris Lahna, a GE manager.

Write to Paul Glader at paul.glader@wsj.com