

Chemed Corporation (CHE)

\$487.26 (As of 02/20/20)

Price Target (6-12 Months): **\$512.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 06/10/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:B

Value: D

Growth: A

Momentum: A

Summary

Chemed exited fourth-quarter 2019 on a solid note, as both earnings and revenues beat estimates. The company witnessed strong revenue growth across key subsidiaries — VITAS and Roto-Rooter. Rise in days-of-care within the VITAS segment and Roto-Rooter's recent acquisitions in CA and franchise territories held by Chemed's largest independent franchisees are impressive. Expansion in both margins during the quarter buoys optimism as well. Over the past year, Chemed's share price has consistently outperformed its industry. However, unfavorable acuity mix shift, fluctuations in net room and board, and contractual adjustments dented the top line in the quarter. Tough competitive landscape and seasonality of business are concerning.

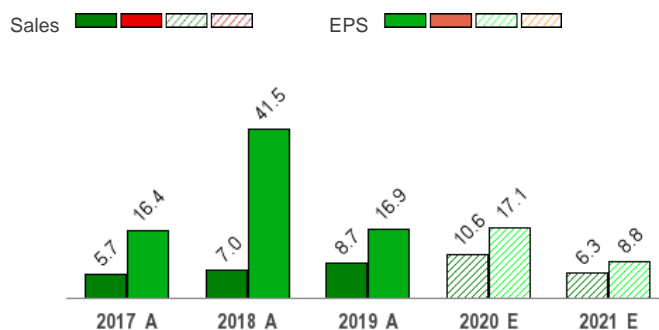
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$513.75 - \$313.49
20 Day Average Volume (sh)	74,350
Market Cap	\$7.8 B
YTD Price Change	10.9%
Beta	1.07
Dividend / Div Yld	\$1.28 / 0.3%
Industry	Medical - Outpatient and Home Healthcare
Zacks Industry Rank	Top 33% (85 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	2.2%
Last Sales Surprise	0.7%
EPS F1 Est- 4 week change	4.2%
Expected Report Date	05/04/2020
Earnings ESP	0.0%
P/E TTM	34.9
P/E F1	29.8
PEG F1	3.4
P/S TTM	4.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	553 E	565 E	571 E	588 E	2,278 E
2020	524 E	531 E	537 E	552 E	2,144 E
2019	462 A	474 A	481 A	522 A	1,939 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$3.93 E	\$4.40 E	\$4.41 E	\$4.93 E	\$17.78 E
2020	\$3.65 E	\$4.06 E	\$4.09 E	\$4.58 E	\$16.34 E
2019	\$2.92 A	\$3.36 A	\$3.46 A	\$4.22 A	\$13.95 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/20/2020. The reports text is as of 02/21/2020.

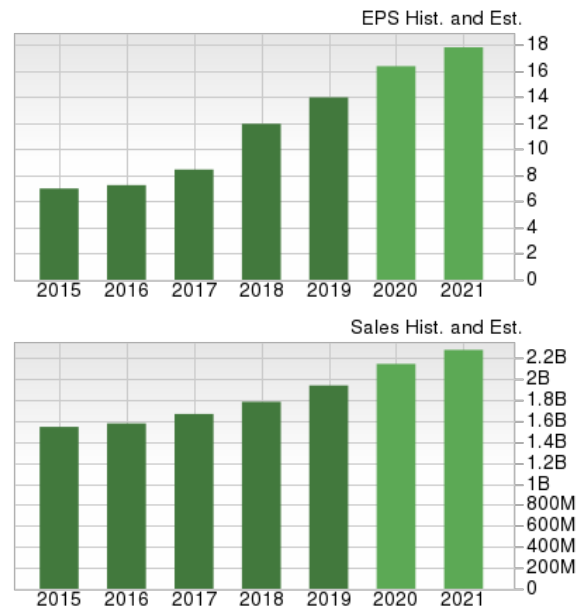
Overview

Cincinnati, OH-based Chemed Corporation purchases, operates and divests subsidiaries engaged in diverse business activities. The company's operating businesses are managed on a decentralized basis. Since its inception, Chemed has engaged in twelve significant acquisitions or divestitures of diverse business units.

Chemed currently operates as two wholly-owned subsidiaries: VITAS Healthcare and Roto-Rooter.

VITAS Healthcare (65.1% of total revenues in 2019; underlying growth rate was 10.8% from 2018): The segment provides hospice and palliative care services for patients with terminal illnesses. This type of care is aimed at making a terminally ill patient's last days as comfortable and pain-free as possible. Hospice care is available for patients who have been initially certified or re-certified as terminally ill (a prognosis of six months or less) by their attending physician, if any, and the hospice physician. VITAS offer all levels of hospice care in a given market, including routine home care, inpatient care and continuous care. Over 95% of VITAS' revenues are derived through Medicare and Medicaid reimbursement programs.

Roto-Rooter (34.9%; up 21.2%): The segment provides plumbing and drain-cleaning services to both residential and commercial customers. This segment provides repair and maintenance services to residential and commercial accounts using the Roto-Rooter registered service marks. Such services include plumbing and sewer, drain and pipe cleaning. They are delivered through company-owned and operated territories, independent contractor-operated territories and franchised locations. This segment also manufactures and sells products and equipment used to provide such services.



Reasons To Buy:

▲ **Share Price Movement:** Over the past year, Chemed's share price has consistently outperformed its industry. The stock has gained 50% compared with the industry's 14.2% rise. It is optimistic to note that in the quarter, the company again registered solid revenue growth both across key subsidiaries. Over the past few quarters, VITAS has been registering expanded average daily census. Meanwhile, the Roto-Rooter business has been seeing growth on strong performance by the core plumbing, excavation and drain cleaning service segments.

Chemed's Roto-Rooter business growth buoys optimism. The company has been registering strong performance from VITAS business over the past few quarters.

▲ **VITAS Prospects Bright:** Chemed has been registering strong performance from VITAS business over the past few quarters.

In the fourth quarter, net revenues at VITAS reflected a rise of 10.7% year over year. The top-line improvement was driven by a 5.5% increase in geographically weighted average Medicare reimbursement rate, 6.1% rise in days-of-care and a rise in Medicare Cap billing limitation that dented revenue growth by 0.3%.

In the fourth quarter, the company's average daily census witnessed an uptick of 6.1% year over year. Total admissions in the quarter registered a 5.4% increase year over year. Starting with the second quarter of 2019, this was the company's third sequential quarter that saw growth in admissions growth rate.

Average revenue per patient per day in the fourth quarter of 2019 saw 5% year-over-year growth. Hospitals admissions increased 5.8%, while home-based admissions rose 1.5%. Admissions within assisted-living facilities increased 9.4% and nursing home admissions grew 0.2% during the quarter.

For 2020, Chemed expects revenue growth of 8.5-9.5% for VITAS (prior to Medicare Cap). Admissions and Average Daily Census in 2020 are expected to grow 3.5-4.5%, whereas High acuity days-of-care are projected at 4.1% of total 2020 days-of-care. It expects \$18-million billing limitations for Medicare Cap in 2020.

▲ **Roto-Rooter Continues to Expand:** Roto-Rooter is currently the nation's leading provider of plumbing and drain cleaning services. Through its network of company-owned branches, independent contractors and franchises, Roto-Rooter offers plumbing and drain cleaning services to over 90% of the U.S. population.

During the fourth quarter, Roto-Rooter witnessed 21.2% growth year over year. Total commercial revenues (including acquisitions) registered growth of 26.4% on a 34.9% rise in drain cleaning revenues and 25.2% improvement in commercial plumbing and excavation. Total residential revenues (including acquisitions) registered growth of 19.4% on a 25.5% rise in residential drain cleaning revenues, an 18.1% improvement in plumbing and excavation, and a 16.3% increase in residential water restoration.

Chemed expects revenue growth of 13-14% for Roto-Rooter in 2020. The projection is based on unit-for-unit revenue growth of 4-5% in core plumbing and drain cleaning services, and continued but slowing revenue growth in water restoration services combined with 12 months of revenues in the Oakland and HSW acquisitions.

We are upbeat about the recently completed acquisition of franchise territories held by the company's largest independent franchisees, serving the Metro Los Angeles area of Inland Empire, San Fernando Valley, San Gabriel County, and Orange County. Additionally, territories in San Diego, CA; Dallas and El Paso, TX; Phoenix, Tucson and Florence, AZ; Salt Lake City, Ogden, Park City and Provo, UT; and Portland and Salem, OR were acquired. These areas (in which Roto-Rooter operates) garner initial aggregate revenues of \$17 million and serve a population of approximately 32 million.

▲ **Returns to Shareholders:** Chemed exited the year with cash and cash equivalents of \$6.2 million, marking a significant improvement from \$4.8 million at the end of 2018. At the end of 2019, cash flow from operating activities was \$301.2 million compared with \$287.1 million at the end of 2018.

Reasons To Sell:

- ▼ **Reimbursement headwind hampering topline growth:** CMS' implementation of a refinement to the Medicare hospice reimbursement per diem (announced in Jan 2016) eliminated the single-tier per diem for routine home care (RHC) and replaced it with a two-tiered rate, with a higher per diem rate for the first 60 days of a hospice patient's care, and a lower rate for day 61 and after. In addition, CMS provided for a Service Intensity Add-on (SIA) payment, which provides for reimbursement of care provided by a registered nurse or social worker for RHC patients within seven days prior to death. The current two-tiered national per diem rate for RHC is \$190.41 for the first 60 days and \$149.68 for RHC provided to patients in hospice beyond 60 days. An individual hospice's actual per diem rate is adjusted for differences in geographic cost of living.
- ▼ **Seasonality of the Business Weigh on the Stock:** A significant portion of the VITAS business operates in the state of Florida. As the majority of Chemed's patients are Medicare recipients, retirees relocating to Florida during the winter months generally result in higher admissions and revenue concentrated only within Florida during that period. Besides, the Roto-Rooter's revenue and operating results are also impacted by significant weather patterns across the U.S. which generally affects the revenue and operating results at Roto-Rooter.
- ▼ **Tough Competitive Landscape:** The market for sewer, drain and pipe cleaning and plumbing repair businesses is highly competitive. Competition is fragmented in most markets with local and regional firms providing much of the competition. Besides, Hospice care in the U.S. is competitive as programs for hospice services are generally uniform. As the hospice care industry is highly fragmented, VITAS compete with a large number of organizations on the basis of its ability to deliver quality, responsive services.
- ▼ **Dependence on Government Mandates:** Over 90% of VITAS' revenues consist of payments from the Medicare and Medicaid programs. The Medicare and Medicaid programs are increasing pressure to control health care costs and cut or limit increases in reimbursement rates for health care services. As with most government programs, the Medicare and Medicaid programs are subject to statutory and regulatory changes, possible retroactive and prospective rate and payment adjustments, administrative rulings, freezes and funding reductions, all of which may adversely affect the level of program payments and have a material adverse effect on VITAS' business. Hence, VITAS' levels of revenues and profitability are subject to the effect of legislative and regulatory changes, including possible reductions in coverage or payment rates or changes in methods of payment, by the Medicare and Medicaid programs.

Headwinds like
seasonality in
business,
competitive
landscape and
dependence on
government
mandates are
intimidating.

Last Earnings Report

Chemed Q4 Earnings & Revenues Beat Estimates, Margins Up

Chemed Corporation reported fourth-quarter 2019 adjusted earnings per share of \$4.22, up 25.9% year over year. The figure beat the Zacks Consensus Estimate by 2.2%.

The company's GAAP (reported) earnings was \$3.96, up 21.5% year over year.

Full-year adjusted earnings was \$13.31, reflecting an 8.8% increase from the year-ago period. However, the company lagged the Zacks Consensus Estimate of \$13.86.

Quarter Ending **12/2019**

Report Date	Feb 18, 2020
Sales Surprise	0.65%
EPS Surprise	2.18%
Quarterly EPS	4.22
Annual EPS (TTM)	13.96

Revenues in Detail

Revenues in the reported quarter improved 14.2% year over year to \$522.3 million, which beat the Zacks Consensus Estimate by 0.6%.

Yearly revenues were \$1.94 billion, reflecting an 8.7% increase from a year ago. However, the metric was in line with the Zacks Consensus Estimate.

Segmental Details

Chemed operates through two wholly-owned subsidiaries, namely VITAS (a major provider of end-of-life care) and Roto-Rooter (a leading commercial and residential plumbing plus drain cleaning service provider).

In the fourth quarter, net revenues at VITAS totaled \$339.9 million, reflecting rise of 10.7% year over year. The top-line improvement was driven by a 5.5% increase in geographically weighted average Medicare reimbursement rate, 6.1% rise in days-of-care and a rise in Medicare Cap billing limitation that dented revenue growth by 0.3%. However, revenue growth was partially offset by acuity mix shift, fluctuations in net room and board and contractual adjustments, the combination of which led to a revenue decline of 0.7% from the prior-year quarter.

Roto-Rooter reported sales of \$182.4 million in the fourth quarter, reflecting growth of 21.2% year over year. On a unit for unit basis, excluding the Oakland and HSW acquisitions completed in July and September 2019, the segment registered revenues of \$162 million for the fourth quarter of 2019 (a year-over-year increase of 7.9%).

Per the company, total commercial revenues (including acquisitions) registered growth of 26.4% on 34.9% rise in drain cleaning revenues, and 25.2% improvement in commercial plumbing and excavation. However, commercial water restoration revenues declined 8.8%.

Total residential revenues (including acquisitions) registered growth of 19.4% on a 25.5% rise in residential drain cleaning revenues, an 18.1% improvement in plumbing and excavation, and a 16.3% increase in residential water restoration.

Margin in Detail

Gross profit rose 20.3% year over year to \$174.9 million in the fourth quarter of 2019. Gross margin expanded 171 basis points (bps) year over year to 33.5%.

Adjusted operating profit grew 16.5% from the year-ago period to \$91.7 million. Moreover, the adjusted operating margin expanded 35 bps to 17.6% on 24.8% escalation in adjusted operating expenses.

Operational Update

Chemed exited the year with cash and cash equivalents of \$6.2 million, marking a significant improvement from \$4.8 million at the end of 2018. The company had long-term debt of \$90 million at the end of 2019, which increased from \$89.2 million at the end of 2018. During the fourth quarter, it repurchased shares worth \$20.7 million.

At the end of 2019, cash flow from operating activities was \$301.2 million compared with \$287.1 million at the end of 2018.

Guidance

For 2020, Chemed expects revenue growth of 8.5-9.5% for VITAS (prior to Medicare Cap). Admissions and Average Daily Census in 2020 are expected to grow 3.5-4.5%, whereas High acuity days-of-care are projected at 4.1% of total 2020 days-of-care. It expects to witness \$18-million billing limitations for Medicare Cap in 2020.

Chemed expects revenue growth of 13-14% for Roto-Rooter in 2020. The projection is based on unit-for-unit revenue growth of 4-5% in core plumbing and drain cleaning services, and continued but slowing revenue growth in water restoration services combined with 12 months of revenues in the Oakland and HSW acquisitions.

For 2020, the company anticipates adjusted earnings (excluding adjustments like non-cash expenses for stock options and tax benefits from stock options) of \$16.20-\$16.50. The Zacks Consensus Estimate for the same is pegged at \$15.67.

Recent News

On **Sep 16, 2019**, Chemed announced that the Roto-Rooter Services Company, a wholly-owned subsidiary of Chemed Corporation, has completed the earlier announced purchase deal of HSW RR, Inc.'s ("HSW") franchise operations and Western Drain Supply for an aggregate purchase price of \$120 million. HSW is Roto-Rooter's largest independent franchise operator.

Valuation

Chemed shares are up 10.9% in the year-to-date period and up 50% in the trailing 12-month period. Stocks in the Zacks sub-industry and Zacks Medical sector are up 10.1% and 2.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 14.2% and up 2.4%, respectively.

The S&P 500 index is up 5.1% in the year-to-date period and up 20.5% in the past year.

The stock is currently trading at 30.6X Forward 12-months earnings, which compares to 21.8X for the Zacks sub-industry, 21.5X for the Zacks sector and 19.4X for the S&P 500 index.

Over the past five years, the stock has traded as high as 52.9X and as low as 16.5X, with a 5-year median 23.9X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$512 price target reflects 32.2x forward 12-months earnings.

The table below shows summary valuation data for CHE.

Valuation Multiples- CHE					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	30.64	21.77	21.46	19.39
	5-Year High	52.88	21.77	21.46	19.39
	5-Year Low	16.45	14.49	15.83	15.18
	5-Year Median	23.88	17.69	18.89	17.47
P/S F12M	Current	3.61	2.53	2.85	3.59
	5-Year High	3.76	2.53	3.83	3.59
	5-Year Low	1.28	0.71	2.45	2.54
	5-Year Median	1.95	0.99	2.97	3.00
P/B TTM	Current	11.60	3.78	4.65	4.68
	5-Year High	12.08	4.08	5.04	4.68
	5-Year Low	4.13	1.91	3.44	2.85
	5-Year Median	6.87	2.47	4.31	3.62

As of 2/20/2020

Industry Analysis Zacks Industry Rank: Top 33% (85 out of 255)



Top Peers

DaVita Inc. (DVA)	Outperform
The Ensign Group, Inc. (ENSG)	Outperform
LHC Group, Inc. (LHCG)	Outperform
Addus HomeCare Corporation (ADUS)	Neutral
Amedisys, Inc. (AMED)	Neutral
Brookdale Senior Living Inc. (BKD)	Neutral
Encompass Health Corporation (EHC)	Neutral
Hanger Inc. (HNGR)	Neutral

Industry Comparison Industry: Medical - Outpatient And Home Healthcare				Industry Peers		
	CHE Neutral	X Industry	S&P 500	AMED Neutral	BKD Neutral	EHC Neutral
VGM Score	B	-	-	B	C	B
Market Cap	7.80 B	915.52 M	24.34 B	6.27 B	1.53 B	8.14 B
# of Analysts	2	2	13	9	3	9
Dividend Yield	0.26%	0.00%	1.78%	0.00%	0.00%	1.36%
Value Score	D	-	-	D	B	B
Cash/Price	0.00	0.06	0.04	0.00	0.25	0.02
EV/EBITDA	28.02	12.40	14.18	36.25	11.59	11.91
PEG Ratio	3.37	2.50	2.09	2.39	NA	2.40
Price/Book (P/B)	10.74	3.44	3.30	9.76	2.20	4.81
Price/Cash Flow (P/CF)	28.26	12.80	13.49	31.24	6.98	13.27
P/E (F1)	29.84	29.83	19.28	38.55	NA	22.54
Price/Sales (P/S)	4.02	1.32	2.68	3.21	0.38	1.77
Earnings Yield	3.35%	2.85%	5.17%	2.60%	-10.37%	4.43%
Debt/Equity	0.24	0.47	0.70	0.45	7.53	1.93
Cash Flow (\$/share)	17.24	1.98	7.03	6.21	1.19	6.22
Growth Score	A	-	-	A	D	B
Hist. EPS Growth (3-5 yrs)	19.50%	12.10%	10.84%	38.47%	NA	16.11%
Proj. EPS Growth (F1/F0)	17.10%	12.84%	7.09%	14.45%	24.19%	-6.31%
Curr. Cash Flow Growth	14.93%	17.33%	6.72%	47.20%	-61.06%	8.30%
Hist. Cash Flow Growth (3-5 yrs)	10.87%	9.79%	8.25%	23.90%	17.11%	13.00%
Current Ratio	0.73	1.23	1.22	1.07	0.57	1.05
Debt/Capital	19.56%	51.70%	42.37%	31.01%	88.28%	67.44%
Net Margin	11.35%	3.19%	11.56%	6.49%	-6.60%	7.79%
Return on Equity	35.38%	16.15%	16.80%	24.95%	-27.40%	23.68%
Sales/Assets	1.66	0.91	0.55	1.61	0.55	0.77
Proj. Sales Growth (F1/F0)	10.59%	5.42%	3.90%	8.73%	-5.89%	6.03%
Momentum Score	A	-	-	B	B	F
Daily Price Chg	-3.93%	0.00%	0.01%	0.16%	-1.19%	-0.30%
1 Week Price Chg	1.41%	1.41%	1.65%	4.83%	4.37%	3.79%
4 Week Price Chg	1.50%	1.03%	0.36%	7.64%	15.78%	4.53%
12 Week Price Chg	12.59%	10.00%	4.39%	17.63%	15.94%	15.68%
52 Week Price Chg	52.75%	11.22%	15.29%	53.20%	11.73%	26.26%
20 Day Average Volume	74,350	101,808	1,992,841	199,856	1,384,799	509,792
(F1) EPS Est 1 week change	4.24%	0.00%	0.00%	0.82%	-0.39%	0.00%
(F1) EPS Est 4 week change	4.24%	0.00%	-0.02%	-0.05%	2.28%	-0.14%
(F1) EPS Est 12 week change	4.88%	0.00%	-0.17%	2.79%	2.28%	-2.18%
(Q1) EPS Est Mthly Chg	3.55%	0.00%	-0.48%	-3.01%	11.54%	-3.48%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	A
Momentum Score	A
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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