

Chemed Corporation (CHE)

\$438.71 (As of 12/27/19)

Price Target (6-12 Months): **\$461.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 06/10/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: C

Growth: A

Momentum: C

Summary

Chemed witnessed solid revenue growth across key subsidiaries — VITAS and Roto-Rooter. A drop in Medicare Cap liability boosted revenue improvement. Rise in days-of-care within the VITAS segment and Roto-Rooter's recent acquisition in CA and franchise territories held by Chemed's largest independent franchisees are impressive. Expansion in the gross margin during the quarter buoys optimism as well. Over the past six months, Chemed's share price has consistently outperformed its industry. Chemed exited third-quarter 2019 on a mixed note, as earnings beat estimates while revenues missed the same. 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.

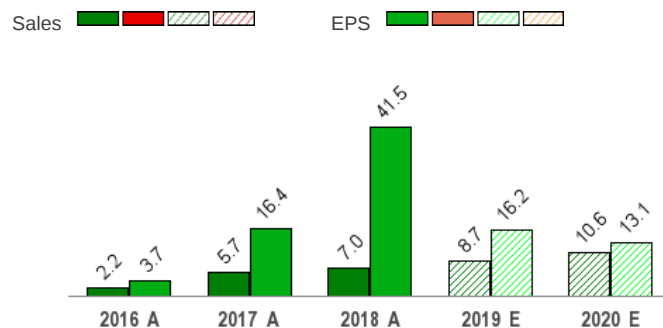
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$445.10 - \$265.08
20 Day Average Volume (sh)	67,937
Market Cap	\$7.0 B
YTD Price Change	54.9%
Beta	1.11
Dividend / Div Yld	\$1.28 / 0.3%
Industry	Medical - Outpatient and Home Healthcare
Zacks Industry Rank	Top 41% (103 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.5%
Last Sales Surprise	-0.9%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/19/2020
Earnings ESP	0.0%
P/E TTM	33.5
P/E F1	31.7
PEG F1	3.6
P/S TTM	3.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	523 E	531 E	537 E	553 E	2,143 E
2019	462 A	474 A	481 A	519 E	1,938 E
2018	439 A	442 A	444 A	458 A	1,783 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$3.52 E	\$3.93 E	\$3.93 E	\$4.43 E	\$15.67 E
2019	\$2.92 A	\$3.36 A	\$3.46 A	\$4.13 E	\$13.86 E
2018	\$2.72 A	\$2.81 A	\$3.07 A	\$3.35 A	\$11.93 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 12/27/2019. The reports text is as of 12/30/2019.

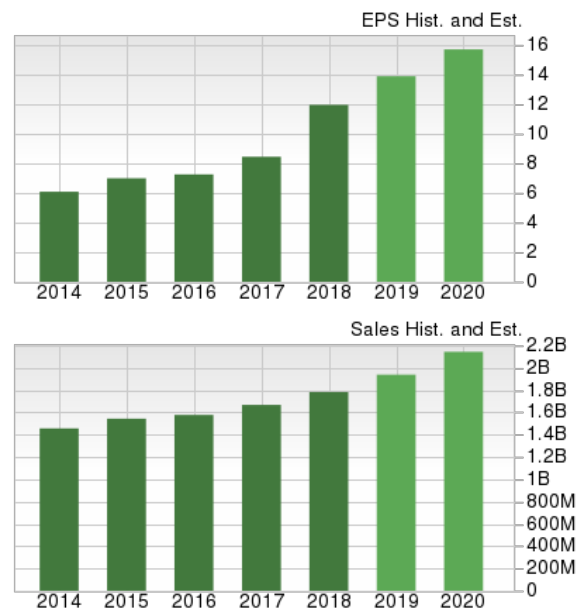
Overview

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 (67.2% of total revenues in 2018; underlying growth rate was 4.3% from 2017): 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 (32.8%; up 12.8%): 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 six months, Chemed's share price has consistently outperformed its industry. The stock has gained 20.3% against the industry's 24.4% decline. It is optimistic to note that the company witnessed solid revenue growth both across its 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 and drain cleaning service segments as well as solid growth in water restoration.

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 third quarter, net revenues at VITAS totaled \$321.7 million, reflecting rise of 6.6% year over year. The top-line improvement was driven by 0.5% growth in geographically-weighted average Medicare reimbursement rate and 6.3% rise in days-of-care.

Chemed also pointed out that VITAS' average length of stay in the third quarter was 92.6 days. Median length of stay was 17 days in the quarter, which is a key indicator of the company's penetration into the high acuity sector of the market. Total admissions witnessed a 4.4% year-over-year increase during the quarter.

For 2019, earlier the company projected VITAS Healthcare revenue growth (prior to Medicare Cap) within 7.5-8%. In 2019, admissions within this segment were anticipated to improve 2.5-3% and Average Daily Census is predicted to rise 5-5.5%. Medicare Cap billing limitations were expected to cap around \$7.8 million.

▲ **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.

Roto-Rooter reported sales growth of 11.6% in the third quarter. Revenues from water restoration increased 3% year over year driven by 19.3% growth in commercial revenues and 6.5% rise in residential revenues.

Roto-Rooter is estimated to report growth of 12-13% in 2019. This revenue estimate includes increased job pricing of around 2%, sustained growth in core plumbing and drain cleaning services as well as slowing consistent revenue growth from water restoration services.

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's capital deployment policy is based on suitable acquisitions and solid return of cash to shareholders through dividends and buybacks. The company exited the third quarter of 2019 with cash and cash equivalents of \$9.1 million, reflecting a significant improvement from \$3.3 million at the end of the second quarter. The company had long-term debt of \$130 million at the end of the third quarter, down from \$85 million at the end of the second quarter. During the third quarter, the company repurchased shares worth \$125 million.

Year-to-date net cash provided by operating activities was \$237.6 million compared with \$230.6 million at the end of the year-ago period.

Reasons To Sell:

- ▼ **Valuation Looks Dull:** Chemed is currently trading at a forward P/E (F12M basis) ratio of 28.1 over the past six months whereas the same for the industry is 19.6 during this period.
- ▼ **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
seasonality
business,
competitive
landscape
dependence
government
mandates
intimidating.

like
in

and
on

are

Last Earnings Report

Chemed Q3 Earnings Surpass Estimates, Revenues Miss

Chemed reported third-quarter 2019 adjusted earnings per share of \$3.46, up 12.7% year over year. The figure beat the Zacks Consensus Estimate by 4.5%.

On a GAAP basis, earnings per share were \$3.56, up 16.3% year over year.

Revenues in the reported quarter improved 8.2% year over year to \$480.6 million but missed the Zacks Consensus Estimate by 0.8%.

Quarter Ending **09/2019**

Report Date	Oct 29, 2019
Sales Surprise	-0.89%
EPS Surprise	4.53%
Quarterly EPS	3.46
Annual EPS (TTM)	13.09

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 third quarter, net revenues at VITAS totaled \$321.7 million, reflecting rise of 6.6% year over year. The top-line improvement was driven by 0.5% growth in geographically weighted average Medicare reimbursement rate and 6.3% rise in days-of-care. A reduction in Medicare Cap liability boosted revenue improvement by 0.2%. Revenue growth was impacted by acuity mix shift, fluctuations in net room and board and contractual adjustments, the combination of which led to a revenue decline of 0.4% from the prior-year quarter.

Roto-Rooter reported sales of \$158.9 million in the third quarter, reflecting growth of 11.6% year over year. Per the company, revenues from water restoration grew 3% year over year to \$25.7 million. The upside was driven by 19.3% year-over-year growth in commercial revenues and 6.5% rise in residential revenues.

Margin in Detail

Gross profit rose 9.8% year over year to \$152.4 million in the third quarter of 2019. Gross margin expanded 46 basis points (bps) year over year to 31.7%. Adjusted operating profit grew 5.5% from the year-ago period to \$75.6 million. However, the adjusted operating margin contracted 41 bps to 15.8% on 14.4% escalation in adjusted operating expenses.

Operational Update

Chemed exited the third quarter of 2019 with cash and cash equivalents of \$9.1 million, marking a significant improvement from \$3.3 million at the end of the second quarter. The company had long-term debt of \$130 million at the end of the third quarter, which rose from \$85 million at the end of the second quarter. During the third quarter, the company repurchased shares worth \$125 million.

Year-to-date net cash provided by operating activities was \$237.6 million compared with \$230.6 million at the end of the year-ago period.

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's shares are up 54.9% in the year-to-date period and the trailing 12-month periods. Stocks in the Zacks sub-industry and Zacks Medical are down 15.8% and up 9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 15.8% and 9%, respectively.

The S&P 500 index is up 27.9% in the year-to-date period in the past year.

The stock is currently trading at 28X Forward 12-months earnings, which compares to 19.6X for the Zacks sub-industry, 21.5X for the Zacks sector and 18.8X 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 of 23X.

Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$461 price target reflects 29.4X 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	28.01	19.63	21.48	18.75
	5-Year High	52.88	20.26	21.48	19.33
	5-Year Low	16.45	14.67	15.91	15.16
	5-Year Median	23.02	17.87	18.97	17.43
P/S F12M	Current	3.28	3.68	2.87	3.41
	5-Year High	3.45	3.68	3.80	3.41
	5-Year Low	1.13	0.73	2.42	2.54
	5-Year Median	1.87	0.96	2.94	3.00
P/B TTM	Current	10.45	6.46	4.61	4.42
	5-Year High	11.32	6.46	5.01	4.42
	5-Year Low	3.81	1.99	3.42	2.85
	5-Year Median	6.69	2.48	4.27	3.60

As of 12/27/2019

Industry Analysis Zacks Industry Rank: Top 41% (103 out of 252)



Top Peers

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

Industry Comparison Industry: Medical - Outpatient And Home Healthcare				Industry Peers		
	CHE Neutral	X Industry	S&P 500	AMED Outperform	BKD Neutral	EHC Neutral
VGM Score	B	-	-	C	C	B
Market Cap	7.02 B	1.00 B	23.80 B	5.35 B	1.30 B	6.88 B
# of Analysts	2	2	13	8	3	8
Dividend Yield	0.29%	0.00%	1.78%	0.00%	0.00%	1.61%
Value Score	C	-	-	D	B	B
Cash/Price	0.00	0.06	0.04	0.00	0.25	0.07
EV/EBITDA	25.42	11.84	13.88	30.93	11.33	11.36
PEG Ratio	3.58	2.44	2.13	2.30	NA	2.04
Price/Book (P/B)	10.45	3.51	3.33	8.87	1.64	4.12
Price/Cash Flow (P/CF)	29.26	12.61	13.55	38.57	2.33	12.13
P/E (F1)	31.69	31.66	19.62	37.75	NA	18.05
Price/Sales (P/S)	3.75	1.20	2.66	2.83	0.31	1.52
Earnings Yield	3.16%	2.59%	5.09%	2.65%	-16.12%	5.53%
Debt/Equity	0.32	0.48	0.71	0.48	6.73	1.94
Cash Flow (\$/share)	15.00	1.98	6.94	4.27	3.02	5.72
Growth Score	A	-	-	B	D	C
Hist. EPS Growth (3-5 yrs)	19.50%	13.13%	10.48%	38.47%	NA	15.79%
Proj. EPS Growth (F1/F0)	16.18%	6.68%	6.14%	21.04%	59.81%	6.44%
Curr. Cash Flow Growth	88.71%	20.39%	14.75%	45.19%	-24.72%	24.32%
Hist. Cash Flow Growth (3-5 yrs)	10.87%	9.79%	8.93%	23.90%	17.11%	10.83%
Current Ratio	0.67	1.09	1.24	0.95	0.59	0.97
Debt/Capital	23.97%	48.25%	42.92%	32.33%	87.07%	67.34%
Net Margin	11.14%	3.35%	11.06%	6.70%	-1.09%	7.07%
Return on Equity	35.06%	15.67%	17.10%	26.53%	-24.04%	23.89%
Sales/Assets	1.71	0.85	0.54	1.75	0.57	0.79
Proj. Sales Growth (F1/F0)	8.73%	4.68%	2.49%	18.52%	-10.03%	7.38%
Momentum Score	C	-	-	F	B	D
Daily Price Chg	0.41%	0.00%	0.21%	1.33%	0.00%	-0.13%
1 Week Price Chg	-1.00%	0.00%	1.46%	-0.18%	4.12%	-1.31%
4 Week Price Chg	1.41%	2.86%	1.98%	-0.19%	-1.82%	-2.69%
12 Week Price Chg	5.91%	8.60%	9.78%	31.90%	-10.23%	11.91%
52 Week Price Chg	55.97%	12.82%	28.47%	44.75%	5.25%	12.82%
20 Day Average Volume	67,937	107,618	1,778,443	203,151	869,349	448,792
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 12 week change	-0.52%	-0.33%	0.12%	6.39%	-8.63%	0.96%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	C
Growth Score	A
Momentum Score	C
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.

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