

H&R Block (HRB)

\$23.65 (As of 01/10/20)

Price Target (6-12 Months): **\$30.00**

Long Term: 6-12 Months

Zacks Recommendation:

Outperform

(Since: 12/06/19)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:B

Value: B

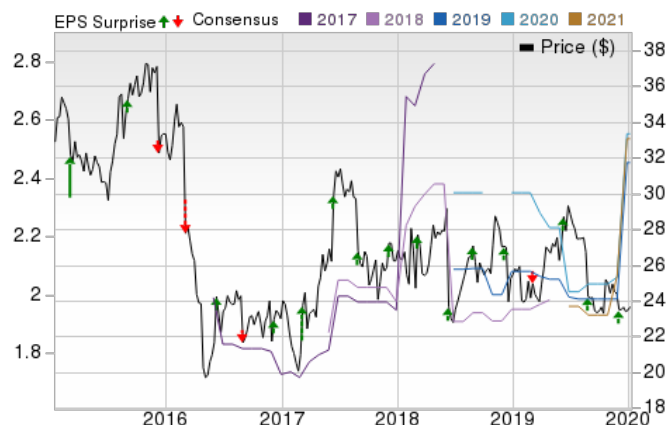
Growth: C

Momentum: D

Summary

H&R Block looks well poised to gain from opportunities offered by the tax industry that has been growing since 2005. The company has undertaken several initiatives to boost both assisted and DIY businesses. The company continues to focus on competitive pricing, investment in product innovation and user experience improvement. The company's solid cash position allows it to pursue opportunities that exhibit true potential and positions it for sustainable clients, revenue and earnings growth. However, escalating costs due to heavy investments in technology and operations might weigh on H&R Block's bottom line, thereby affecting its share price, which has underperformed its industry year to date. Seasonality causes considerable fluctuations in revenues and makes profit forecasting difficult. The company also faces huge litigations.

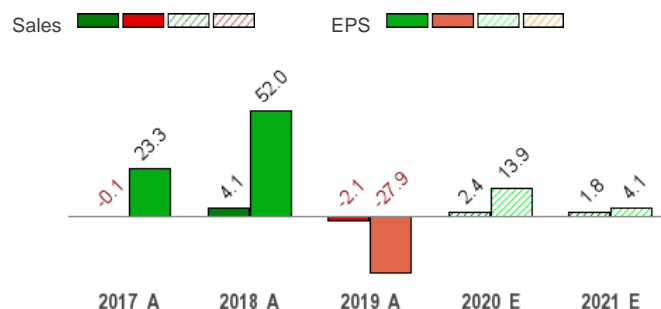
Price, Consensus & Surprise



Data Overview

| | |
|----------------------------|---|
| 52 Week High-Low | \$29.62 - \$22.79 |
| 20 Day Average Volume (sh) | 2,706,195 |
| Market Cap | \$4.6 B |
| YTD Price Change | 0.7% |
| Beta | 0.22 |
| Dividend / Div Yld | \$1.04 / 4.4% |
| Industry | Consumer Services - Miscellaneous |
| Zacks Industry Rank | Top 15% (38 out of 254) |

Sales and EPS Growth Rates (Y/Y %)



| | |
|---------------------------|-------------------|
| Last EPS Surprise | 6.6% |
| Last Sales Surprise | -1.6% |
| EPS F1 Est- 4 week change | 0.0% |
| Expected Report Date | 03/05/2020 |
| Earnings ESP | 0.0% |
| P/E TTM | 10.9 |
| P/E F1 | 9.7 |
| PEG F1 | 1.0 |
| P/S TTM | 1.5 |

Sales Estimates (millions of \$)

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|------|-------|-------|-------|---------|---------|
| 2021 | | | | | 3,225 E |
| 2020 | 150 A | 161 A | 489 E | 2,376 E | 3,168 E |
| 2019 | 145 A | 149 A | 468 A | 2,332 A | 3,095 A |

EPS Estimates

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|------|-----------|-----------|-----------|----------|----------|
| 2021 | -\$0.79 E | -\$0.97 E | -\$0.55 E | \$3.28 E | \$2.55 E |
| 2020 | -\$0.72 A | -\$0.85 A | -\$0.54 E | \$4.56 E | \$2.45 E |
| 2019 | -\$0.72 A | -\$0.83 A | -\$0.58 A | \$4.32 A | \$2.15 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 01/10/2020. The reports text is as of 01/13/2020.

Overview

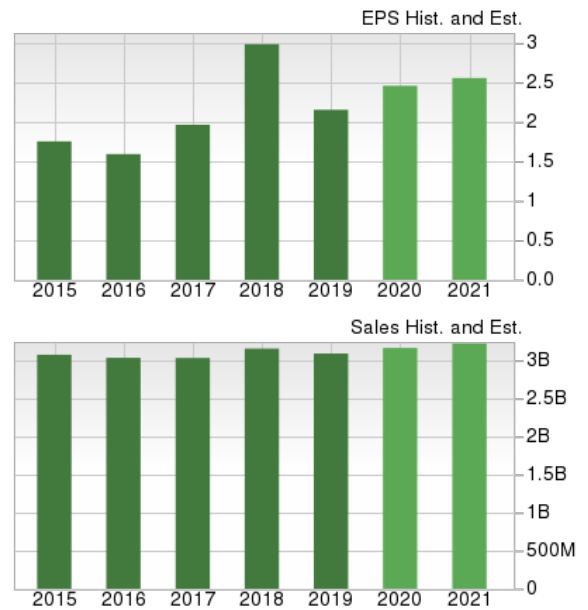
H&R Block Inc. is a leading provider of tax preparation services. The company provides assisted income tax return preparation, do-it-yourself (DIY) tax solutions and other products and services associated with income tax return preparation in the United States, Canada and Australia.

Assisted income tax return preparation services are provided through a system of retail offices operated directly by the company or by franchisees. DIY tax services include preparation of federal and state income tax returns, advice and tax-related news, access to tax tips, use of calculators for tax planning, and error checking and electronic filing. The company develops and markets DIY income tax preparation software online, and through third-party retail stores and direct mail. The company offers return preparation solutions through mobile applications as well.

Additional offerings from the company include Refund Transfers, H&R Block Emerald Advance lines of credit, Peace of Mind Extended Service Plan, Tax Identity Shield, H&R Block Emerald Prepaid MasterCard, and refund advance loans; POM, an Instant Cash Back refund option; and H&R Block Pay with Refund option.

H&R Block was organized as a corporation in 1955 under the laws of the State of Missouri and is headquartered in Kansas City, MO. The company has around 11,600 company-owned and franchise offices worldwide. As most of the clients file their tax returns from January through April of each year, most of H&R Block's revenues from income tax return preparation and related services and products are received during this period. As a result, the Tax Services segment generally operates at a loss through the first nine months of a fiscal year.

In fiscal 2018, the company's revenues increased \$4.1% on a year-over-year basis. U.S. assisted tax preparation fees were up 2.4%, driven by an increase of 0.7% in tax returns prepared in company-owned offices, and a more favorable pricing and mix. Franchise returns were down 3.4% mainly due to acquisition of franchise businesses during the year, which resulted in a decline 1.9% in U.S royalties. U.S. DIY tax preparation fees increased 11% and international revenues increased 8.1. Fees earned on RTs were up 16%, due to a price surge on RTs in assisted business.



Reasons To Buy:

▲ **The tax industry is growing** steadily since 2005 in both assisted and DIY channels and the momentum is expected to continue in the years to come. H&R Block looks well poised to gain from opportunities offered by the industry. In its assisted business, the company is focused on investment in price, developing and delivering on a clear brand promise, enhancing the quality service delivery. In the DIY business, H&R Block continues focusing on competitive pricing and investment in product innovation and user experience improvement.

H&R Block looks well poised to gain from opportunities offered by growing tax industry in both assisted and DIY channels.

▲ **H&R Block is investing** in three broad areas in 2019 — price, technology, and operational excellence. On the price front, it is focusing on price reduction to attain competitive pricing. With technology, H&R Block is building a new tax engine to consolidate multiple systems, invest in cross-channel capabilities to streamline client experience across platforms, move its physical data centers to the cloud, and optimize data architecture and analytics platform. With regard to operational excellence, the company is trying to improve execution of standard operating procedures for better quality and consistency of service delivery. These initiatives are aimed at achieving overall objectives of clients, revenue, and earnings growth over the long term.

▲ H&R Block has a **robust cash generation capacity**, which allows it to pursue opportunities that exhibit true potential and positions it for sustainable clients, revenue and earnings growth. The company used \$209.5 million of cash in operating activities and spend \$27.7 million on capex in second-quarter fiscal 2020.

Risks

- H&R Block is witnessing **escalation in costs** as it plans to invest heavily in technology and operations. This might weigh on the company's bottom line, thereby affecting its share price, that has declined 7.5% over the past year compared with 5.1% loss of the industry it belongs to. The company earns majority of its revenues in the fourth quarter of the fiscal year as most of its clients file their tax returns from February through April. Revenues stay significantly down and the company incurs loss in first three quarters of fiscal year.
 - H&R Block **faces huge litigations** in connection with its various operating activities. H&R Block is also exposed to employment related lawsuits in various parts of the country and compliance fee litigation in Missouri state and federal courts. Such litigations weigh on investor sentiment and hamper the company's goodwill.
 - H&R Block's **balance sheet is highly leveraged**. As of Oct 31, 2019, long-term debt and line of credit borrowings were \$1.3 billion while cash and cash equivalents were \$245.31 million. Such a cash position implies that H&R Block needs to generate adequate amount of operating cash flow to service its debt. Also, high debt may limit the company's future expansion and worsen its risk profile.
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Last Earnings Report

H&R Block Q2 Loss Widens Year Over Year

H&R Block incurred second-quarter fiscal 2020 adjusted loss per share from continuing operations of 85 cents, lower than the Zacks Consensus Estimate of loss of 91 cents.

Loss increased 2.4% year over year due to rise in pre-tax loss (12.6% year over year to \$261.3 million) and lower shares outstanding, partially offset by an increased tax benefit. The company usually incurs loss in the first three quarters of any fiscal year due to the seasonality of its tax business.

Quarter Ending **10/2019**

| Report Date | Dec 04, 2019 |
|------------------|--------------|
| Sales Surprise | -1.59% |
| EPS Surprise | 6.59% |
| Quarterly EPS | -0.85 |
| Annual EPS (TTM) | 2.17 |

Revenues

Revenues of \$160.8 million lagged the consensus estimate by 1.2% and increased 8% year over year. The improvement was driven by contribution from Wave Financial acquisition and improved tax return volumes.

Expenses

Total operating expenses were \$403.5 million, 10.8% higher year over year. The increase was due to technology and Wave Financial related investments, and legal expenses, partially offset by lower occupancy costs.

Financial Position

H&R Block exited the quarter with cash and cash equivalents of \$245.3 million compared with \$607.7 million at the end of the prior quarter. Long-term debt and line of credit borrowings were \$1.3 billion. The company used \$209.5 million of cash in operating activities and capex was \$27.7 million.

The company paid out dividends of \$51.6 million in the quarter. A cash dividend of 26 cents per share is payable Jan 2, 2020, to shareholders of record as of Dec 9, 2019. H&R Block repurchased and retired around 5.7 million shares at an aggregate price of \$136.9 million.

Outlook

The company reaffirmed its fiscal 2020 revenue growth and margin outlook. It continues to expect total revenue growth of 1.5% to 3.5%. EBITDA margin is expected between 24% and 26%. The company revised its effective tax rate expectation to 19-21% from 23-25%.

Recent News

On **Nov 7, 2019**, H&R Block's board of directors declared a quarterly cash dividend of 26 cents per share, payable on Jan 2, 2019, to shareholders of record as of Dec 9, 2019.

On **Nov 7, 2019**, H&R Block announced the appointment of Anuradha Gupta to its board of directors, effective immediately.

Valuation

H&R Block shares are down 7.5% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 5.1%, while those in the Zacks Business Services sector are up 28.8%, over the past year.

The S&P 500 index is up 25.6% in the past year.

The stock is currently trading at 9.38X price to forward 12 months' earnings, which compares to 13.53X for the Zacks sub-industry, 20.25X for the Zacks sector and 18.88X for the S&P 500 index.

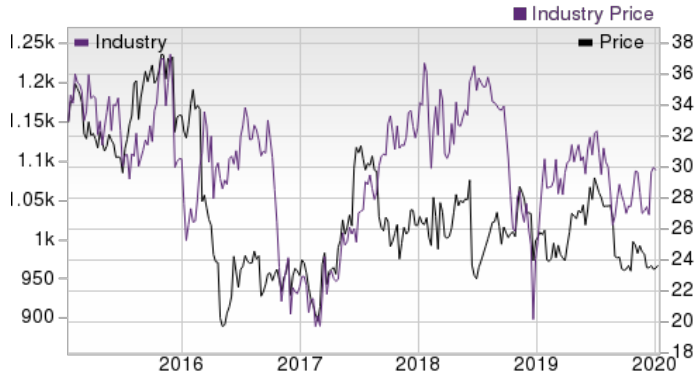
Over the past five years, the stock has traded as high as 17.5X and as low as 9.27X, with a 5-year median of 13.32X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$30.00 price target reflects 11.9X price to forward 12 months' earnings.

The table below shows summary valuation data for HRB

| Valuation Multiples - HRB | | | | | |
|---------------------------|---------------|-------|--------------|--------|---------|
| | | Stock | Sub-Industry | Sector | S&P 500 |
| P/E F 12M | Current | 9.38 | 13.53 | 20.25 | 18.88 |
| | 5-Year High | 17.50 | 22.1 | 23.34 | 19.34 |
| | 5-Year Low | 9.27 | 13.53 | 16.17 | 15.17 |
| | 5-Year Median | 13.32 | 17.85 | 20.09 | 17.44 |
| P/S F12M | Current | 1.44 | 0.64 | 2.35 | 3.5 |
| | 5-Year High | 3.2 | 2.61 | 3.19 | 3.5 |
| | 5-Year Low | 1.39 | 0.64 | 1.81 | 2.54 |
| | 5-Year Median | 1.78 | 1.66 | 2.54 | 3 |
| EV/EBITDA TTM | Current | 8.35 | 9.36 | 12.75 | 11.99 |
| | 5-Year High | 12.61 | 10.01 | 17.77 | 12.86 |
| | 5-Year Low | 4.91 | 6.41 | 11.08 | 8.48 |
| | 5-Year Median | 7.33 | 7.92 | 12.43 | 10.67 |

As of 01/10/2020

Industry Analysis Zacks Industry Rank: Top 15% (38 out of 254)



Top Peers

| | |
|---|---------|
| Blucora, Inc. (BCOR) | Neutral |
| Broadridge Financial Solutions, Inc. (BR) | Neutral |
| Equifax, Inc. (EFX) | Neutral |
| East West Bancorp, Inc. (EWBC) | Neutral |
| Fiserv, Inc. (FISV) | Neutral |
| Global Payments Inc. (GPN) | Neutral |
| Intuit Inc. (INTU) | Neutral |
| Paychex, Inc. (PAYX) | Neutral |

| Industry Comparison Industry: Consumer Services - Miscellaneous | | | | Industry Peers | | |
|---|----------------|------------|-----------|----------------|--------------|--------------|
| | HRB Outperform | X Industry | S&P 500 | EFX Neutral | INTU Neutral | PAYX Neutral |
| VGM Score | B | - | - | F | F | C |
| Market Cap | 4.62 B | 962.48 M | 24.03 B | 17.77 B | 71.65 B | 30.52 B |
| # of Analysts | 3 | 4 | 13 | 11 | 11 | 11 |
| Dividend Yield | 4.40% | 0.00% | 1.78% | 1.06% | 0.77% | 2.91% |
| Value Score | B | - | - | D | D | D |
| Cash/Price | 0.09 | 0.05 | 0.04 | 0.01 | 0.03 | 0.02 |
| EV/EBITDA | 6.89 | 11.74 | 14.04 | 26.34 | 33.03 | 17.28 |
| PEG Ratio | 0.97 | 1.37 | 2.02 | 2.93 | 2.32 | 3.92 |
| Price/Book (P/B) | NA | 2.58 | 3.32 | 6.94 | 19.72 | 11.88 |
| Price/Cash Flow (P/CF) | 7.94 | 10.72 | 13.52 | 17.38 | 42.15 | 21.29 |
| P/E (F1) | 9.71 | 14.35 | 18.82 | 25.39 | 36.33 | 27.44 |
| Price/Sales (P/S) | 1.48 | 0.99 | 2.63 | 5.17 | 10.33 | 7.57 |
| Earnings Yield | 10.36% | 6.99% | 5.31% | 3.94% | 2.75% | 3.65% |
| Debt/Equity | -17.25 | 0.23 | 0.72 | 1.11 | 0.18 | 0.35 |
| Cash Flow (\$/share) | 2.98 | 2.61 | 6.94 | 8.44 | 6.53 | 4.01 |
| Growth Score | C | - | - | F | F | C |
| Hist. EPS Growth (3-5 yrs) | 8.76% | 7.03% | 10.56% | 8.15% | 24.52% | 10.85% |
| Proj. EPS Growth (F1/F0) | 14.11% | 7.89% | 7.49% | 3.60% | 12.23% | 9.41% |
| Curr. Cash Flow Growth | -24.47% | 14.35% | 14.83% | 0.23% | 18.22% | 10.82% |
| Hist. Cash Flow Growth (3-5 yrs) | 1.16% | 10.77% | 9.00% | 9.86% | 9.68% | 12.37% |
| Current Ratio | 0.48 | 0.95 | 1.23 | 0.57 | 1.80 | 1.17 |
| Debt/Capital | 86.00% | 46.91% | 42.99% | 52.56% | 15.57% | 25.87% |
| Net Margin | 13.28% | 1.85% | 11.08% | -11.13% | 22.79% | 26.72% |
| Return on Equity | 332.04% | 10.72% | 17.16% | 24.39% | 42.04% | 41.21% |
| Sales/Assets | 1.06 | 1.10 | 0.55 | 0.47 | 1.12 | 0.44 |
| Proj. Sales Growth (F1/F0) | 2.36% | 2.93% | 4.20% | 5.68% | 10.73% | 10.17% |
| Momentum Score | D | - | - | F | D | B |
| Daily Price Chg | 0.85% | 0.20% | -0.33% | -0.85% | 0.13% | -0.55% |
| 1 Week Price Chg | 0.30% | 0.28% | -0.30% | 1.90% | -1.00% | -0.35% |
| 4 Week Price Chg | 0.60% | 3.87% | 1.71% | 5.91% | 8.90% | 0.63% |
| 12 Week Price Chg | -0.30% | 6.94% | 6.05% | 0.01% | 3.27% | 0.64% |
| 52 Week Price Chg | -7.62% | 2.47% | 22.39% | 51.79% | 33.58% | 26.49% |
| 20 Day Average Volume | 2,706,195 | 122,871 | 1,580,816 | 604,816 | 1,117,136 | 1,404,620 |
| (F1) EPS Est 1 week change | 0.00% | 0.00% | 0.00% | -0.03% | 0.00% | 0.00% |
| (F1) EPS Est 4 week change | 0.00% | 0.00% | 0.00% | -0.76% | 0.00% | 0.01% |
| (F1) EPS Est 12 week change | 23.59% | 2.53% | -0.50% | -3.86% | 0.16% | -0.01% |
| (Q1) EPS Est Mthly Chg | 0.00% | 0.00% | 0.00% | -0.81% | 0.00% | -1.73% |

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 | B |
| Growth Score | C |
| Momentum Score | D |
| 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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