

Service Corporation(SCI)

\$46.54 (As of 08/06/20)

Price Target (6-12 Months): **\$49.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 04/07/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: B

Summary

Service Corporation's shares have rallied 21% in the past three months, almost in line with the industry. The company has been gaining on increased funerals performed due to higher deaths amid coronavirus, which along with cost management aided its performance in second-quarter 2020. Also, the company's focus on expansion of funeral homes is noteworthy. During the quarter, both earnings and revenues improved year over year and beat the consensus mark. However, preneed sales remained soft due to increased stay-at-home and social-distancing orders. Though the company expects high funeral services performed amid the pandemic, reduced funeral size due to curbs on gatherings is expected to continue weighing on average revenue per service. While the company is focused on cost-control, costs are likely to remain elevated in 2020 due to COVID-19.

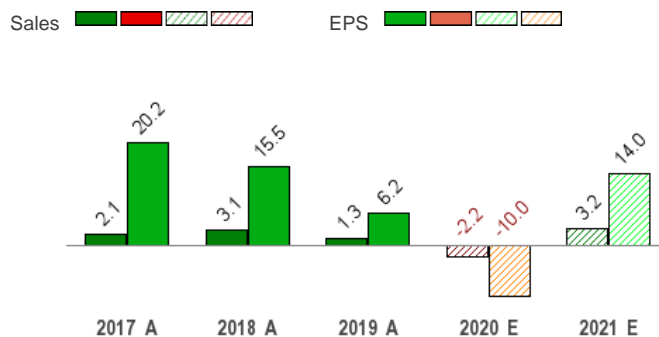
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$52.89 - \$33.93
20 Day Average Volume (sh)	1,285,044
Market Cap	\$8.2 B
YTD Price Change	1.1%
Beta	0.75
Dividend / Div Yld	\$0.76 / 1.6%
Industry	Funeral Services
Zacks Industry Rank	Bottom 49% (129 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	141.7%
Last Sales Surprise	15.5%
EPS F1 Est- 4 week change	32.0%
Expected Report Date	11/04/2020
Earnings ESP	0.0%
P/E TTM	23.5
P/E F1	27.2
PEG F1	2.4
P/S TTM	2.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	810 E	830 E	786 E	864 E	3,260 E
2020	803 A	820 A	765 E	841 E	3,160 E
2019	798 A	813 A	769 A	851 A	3,231 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.48 E	\$0.49 E	\$0.40 E	\$0.59 E	\$1.95 E
2020	\$0.43 A	\$0.58 A	\$0.39 E	\$0.55 E	\$1.71 E
2019	\$0.47 A	\$0.47 A	\$0.37 A	\$0.60 A	\$1.90 A

*Quarterly figures may not add up to annual.

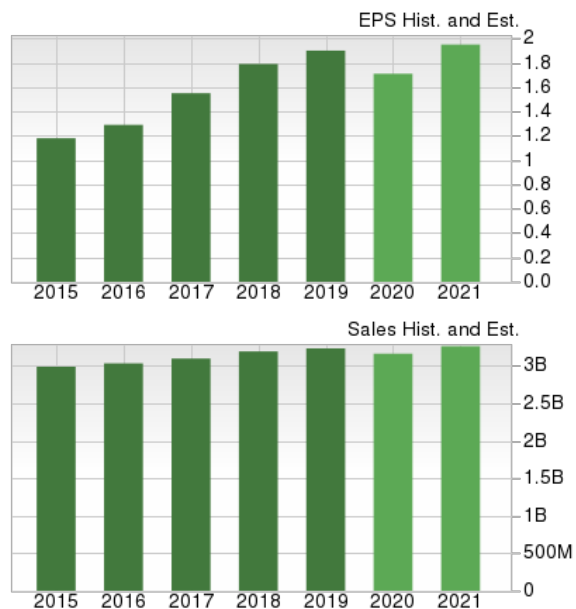
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/06/2020. The reports text is as of 08/07/2020.

Overview

Known for its transcontinental brand namely Dignity Memorial, Service Corporation International has been strengthening its funeral and cemetery businesses for a while now. Notably, the company had a market share of 15-16% in North America's death care industry in 2019. With a wide repertoire of funeral service and cemetery operations, the company remains well-positioned to take advantage of the aging Baby Boomer generation. In this context, Service Corporation's funeral service locations, cemeteries, funeral service/cemetery combination locations, crematoria and other related businesses spread across geographies are noteworthy. Additionally, the company's active acquisition efforts, including 15 funeral homes and seven cemeteries in June 2018, have been accretive.

Further, Service Corporation's cemeteries offer cemetery property interment rights, including developed lots, mausoleum spaces, lawn crypts, niches, and other cremation memorialization and interment options. Additionally, cemetery merchandise and services, which includes memorial markers and bases, graveside services, flowers and floral placement, other ancillary merchandise, as well as interments among others, are provided at Service Corporation's cemeteries.

As of December 31, 2019, Service Corporation operated 1,471 funeral service locations and 482 cemeteries across 44 states, eight provinces in Canada, the District of Columbia and Puerto Rico. Markedly, cemeteries include 290 funeral service/cemetery combination locations.



Reasons To Buy:

▲ **Solid Q2 Results:** Shares of Service Corporation have rallied 21% in the past three months, almost in line with the industry. The company has been gaining on increased funerals performed due to the coronavirus pandemic, which along with strong cost management aided its performance in second-quarter 2020. During the quarter, both earnings and revenues improved year over year and surpassed the Zacks Consensus Estimate. The bottom line was backed by increased gross profit stemming from greater funeral services performed in the core funeral services business on account of the pandemic, along with solid cost management. Management stated that it saw a better-than-anticipated operating performance in its funeral and cemetery operations. Increased funeral and cemetery revenues aided the top line. Core revenues in both segments increased but was partly countered by a decline in preneed sales.

The company remains committed toward pursuing strategic buyouts and building new funeral homes to generate greater returns. Further, increased funerals amid the pandemic are aiding revenues.

Management expects continued effects of the pandemic to lead to higher funeral services performed, especially in the early third quarter.

▲ **Robust Cemetery Revenues:** Revenues in the segment rose 1.6% to \$339.1 million, thanks to a jump in core revenues. Core revenues gained from higher atneed revenues, partly offset by a fall in total recognized preneed revenues. Comparable Cemetery revenues improved 1.7% year over year on the back of higher atneed revenues, which stemmed from a rise in services performed. Comparable preneed cemetery sales production grew 10.4%, thanks to productive virtual tools, increased sales incentives and greater leads from atneed services along with gradual relaxation of bans on gatherings in several states.

▲ **Focus on Expansion:** The company remains committed toward pursuing strategic buyouts for both its segments and building new funeral homes to generate greater returns. During the second quarter, the company incurred capital expenditures of \$52.6 million. These were directed toward capital enhancements at currently operating locations, development of cemetery property and expenditures for construction of new funeral service locations. These investments are touted to be accretive to the company in the near term. Management remains focused on seeking acquisition opportunities. Moreover, the company anticipates spending capital on new funeral homes and expansion opportunities to increase its footprint. In 2020, expenditures associated with capital enhancements at current locations and cemetery development are anticipated in a band of \$165-\$195 million.

In 2018, the company deployed approximately \$200 million towards acquisitions. Some notable acquisitions made by the company in the past include Alderwoods Group, Keystone North America, The Neptune Society, and Stewart Enterprises. Also, buyouts in the cemetery segment are aimed at exploiting increased opportunities to cater to Baby Boomers.

▲ **Shareholder-Friendly Moves:** Service Corporation's strong cash flow helps it undertake efficient capital allocation. The company remains focused on enhancing shareholders' value via dividend payments and share repurchases. Notably, Service Corporation's dividend rate has increased from 2.5 cents per share in 2005 to 19 cents in 2020. The company currently has a dividend payout ratio of 38.4%, dividend yield of 1.6% and free cash flow yield of 6.9%. With an annual free cash flow return on investment of 8.7%, the dividend payment is likely to be sustainable. Well, the company has a targeted dividend payout ratio of 30-40% of earnings.

Also, the company has been focused on making share buybacks. In the first half of 2020, Service Corporation repurchased 5,117,807 shares for \$210.6 million. Even after Jun 30, the company repurchased 791,744 shares and had shares worth \$75.8 million available under its buyback authorization. We note that the company had cash and cash equivalents of \$222.3 million, while its short-term debt stood at \$87.3 million as of Jun 30, 2020.

Reasons To Sell:

- ▼ **Stock Looks Overvalued:** Considering the price-to-earnings (P/E) ratio, Service Corporation looks overvalued when compared with the industry. The stock has a trailing 12-month P/E ratio of 23.51, which is below its high level of 27.66 scaled in a year. Meanwhile, the trailing 12-month P/E ratio for the industry and S&P 500 index is currently pegged at 17.66 and 23.5, respectively.
- ▼ **Elevated Costs:** Service Corporation is witnessing elevated costs, especially amid COVID-19 pandemic. During the second quarter of 2020, corporate general and administrative costs escalated \$8 million to \$37.2 million, somewhat due to a rise in incentive compensation costs, including bonuses for some front-line workers, and costs related to community outreach efforts. While the company is focused on cost-containment measures, it expects a modest increase in costs and expenses, corresponding to stay-at-home orders as well as restrictions on gatherings.
- ▼ **Soft Preneed Sales Amid COVID-19:** Although Service Corporation's revenues increased in the second quarter of 2020 due to increased deaths amid the pandemic, the company's preneed sales remained soft in both segments. In the Funeral segment, comparable funeral revenues slipped 1.2% year over year due to a fall in recognized preneed revenues and other revenues, stemming from a decline in preneed funeral sales production. Comparable preneed funeral sales production tumbled 27.3% due to a fall in preneed production in the non-funeral home channel as well as a decline in core funeral locations, both of which were affected by increased stay-at-home and social-distancing orders. Even in the Cemetery segment, total recognized preneed revenues dropped due to lower recognized preneed merchandise and service revenues.

Reduced preneed sales due to increased stay-at-home and social-distancing orders amid the pandemic are a concern for Service Corporation. Also, costs are likely to remain high.

Apart from this, results of the company were partly hampered by a decline in funeral average per case due to bans on big gatherings. Though the company expects to perform increased funeral services amid the pandemic, it anticipates lower average revenue per service (stemming from curbs on gatherings, together with self-quarantine measures in certain jurisdictions) to remain a headwind. Also, management said that it might start witnessing a slowdown as the spikes in death cases (related to the pandemic) in the last five months were mostly ahead of time.

- ▼ **Stiff Competition:** The funeral and cemetery industry is quite competitive in North America. The company competes with various locally-owned, independent operators on grounds of standard, products and pricing.

In fact, the company has faced pricing pressure in the past from independent funeral service location and cemetery operators, monument dealers, casket retailers, low-cost funeral providers and more. Also, use of alternative channels, such as e-commerce, to buy funeral related products has increased competition. Failure to keep up with the pressure may hurt the company's financial results and cash flow.

Last Earnings Report

Service Corporation Q2 Earnings Top Estimates, Rise Y/Y

Service Corporation reported second-quarter 2020 adjusted earnings of 58 cents per share, which came way ahead of the Zacks Consensus Estimate of 24 cents. Further, the bottom line jumped 23% from the year-ago quarter's reported figure on the back of increased gross profit stemming from greater funeral services performed in the core funeral services business on account of the pandemic, along with solid cost management. Management stated that it saw a better-than-anticipated operating performance in its funeral and cemetery operations. Results were somewhat offset by reduced funeral average per case. For 2020, Service Corporation envisions adjusted earnings per share of \$1.78-\$2. The company's earnings came in at \$1.90 in 2019.

Quarter Ending **06/2020**

Report Date	Jul 29, 2020
Sales Surprise	15.47%
EPS Surprise	141.67%
Quarterly EPS	0.58
Annual EPS (TTM)	1.98

Total revenues of \$820 million inched up 0.9% from \$812.6 million in the year-ago quarter, backed by increased funeral and cemetery revenues. Moreover, the figure beat the consensus mark of \$710 million. Corporate general and administrative costs escalated \$8 million to \$37.2 million, while it grew \$6.4 million on excluding last year's legal expense adjustments. Apart from this, these costs increased due to a rise in incentive compensation costs, including bonuses for some front-line workers, along with costs related to community outreach efforts. The company's interest costs fell \$5.6 million to \$41.8 million in the quarter.

Segment Discussion

Consolidated **Funeral** revenues grew 0.4% to \$480.9 million on higher core revenues. Core revenues gained from a rise in atneed as well as matured preneed revenues. Further, non-funeral home revenues improved year over year, while recognized preneed revenue saw a decline of 30.2% to \$27.7 million.

Comparable funeral revenues slipped 1.2% year over year due to a fall in recognized preneed revenues and other revenues, stemming from a decline in preneed funeral sales production. These were partly compensated by a rise in core funeral revenues, which was backed by increased core funeral services performed largely due to coronavirus-led deaths. This was somewhat negated by a fall in core average revenue per service, which results from social-distancing measures that led to smaller and lesser funeral memorial services. Moreover, the core cremation rate rose 210 basis points on account of a temporary shift toward direct cremation amid the pandemic. Comparable preneed funeral sales production tumbled 27.3% due to a fall in preneed production in the non-funeral home channel as well as a decline in core funeral locations, both of which were affected by increased stay-at-home and social-distancing orders.

Comparable funeral gross profit elevated 23.4% to \$112.9 million. Also, the gross profit margin increased 480 basis points to 24%, courtesy of core business growth and pandemic-led cost-containment efforts, partly negated by a fall in lower-margin revenue channels.

Consolidated **Cemetery** revenues rose 1.6% to \$339.1 million, thanks to a jump in core revenues. Core revenues gained from higher atneed revenues, partly offset by a fall in total recognized preneed revenues stemming from lower recognized preneed merchandise and service revenues.

Comparable Cemetery revenues improved 1.7% year over year on the back of higher atneed revenues, which stemmed from a rise in services performed. This was somewhat countered by a decline in recognized preneed merchandise and service revenues. Comparable preneed cemetery sales production grew 10.4%, thanks to productive virtual tools, increased sales incentives and greater leads from atneed services along with gradual relaxation of bans on gatherings in several states.

Comparable cemetery gross profit climbed 2.4% to \$102.8 million and the respective margin expanded 10 bps to 30.3%. The upside can be attributable to higher cemetery revenues together with cost-curtailments undertaken in late March and early April due to the COVID-19 outbreak. This was partly countered by increased selling compensation-related expenses.

Other Financial Details & Outlook

The company ended the quarter with cash and cash equivalents of \$222.2 million, long-term debt of \$3,573.7 million and total equity of \$1,754.3 million. Net cash provided by operating activities amounted to \$364.3 million in the first six months of 2020 compared with \$262.9 million in the prior-year period. During the second quarter, the company incurred capital expenditures of \$52.6 million. Further, the company expects net cash from operating activities to be \$600-\$660 million, on excluding certain special items. Expenditures associated with capital enhancements at current locations and cemetery development are anticipated in a band of \$165-\$195 million for 2020.

Management expects continued effects of the pandemic to lead to higher funeral services performed, especially in the early third quarter. This is likely to be partly countered by lower average revenue per service, stemming from curbs on gatherings, together with self-quarantine measures in certain jurisdictions. Further, Service Corporation anticipates preneed sales to move somewhat in line with atneed services, partly due to family members who prefer to book cemetery properties close to their loved ones.

That said, management noted that the company might start witnessing a slowdown in funeral services as the spike in death cases (related to the pandemic) in the last five months is mostly ahead of time. While the company is focused on cost-containment measures, it expects a modest increase in costs and expenses, corresponding to stay-at-home orders as well as restrictions on gatherings.

Recent News

Service Corporation Declares Dividend – May 13, 2020

Service Corporation has approved its quarterly cash dividend of 19 cents per share. This will be payable on Jun 30, 2020 to shareholders of record as on Jun 15.

Valuation

Service Corporation's shares are up 1.1% in the year-to-date period and down 0.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are down 5.4% and 8.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 2.8% and 6.4%, respectively.

The S&P 500 index is up 4% in the year-to-date period and up 14.4% in the past year.

The stock is currently trading at 25.91X forward 12-month earnings, which compares to 18.89X for the Zacks sub-industry, 19.9X for the Zacks sector and 22.84X the S&P 500 index.

Over the past five years, the stock has traded as high as 25.91X and as low as 16.39X, with a 5-year median of 21.59X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$49 price target reflects 27.28X forward 12-month earnings.

The table below shows summary valuation data for SCI

Valuation Multiples -SCI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	25.91	18.89	19.9	22.84
	5-Year High	25.91	23.78	22.37	22.84
	5-Year Low	16.39	14.07	16.63	15.25
	5-Year Median	21.59	18.04	19.57	17.55
P/S F12M	Current	2.6	1.8	9.41	3.66
	5-Year High	2.85	2.19	11.15	3.66
	5-Year Low	1.37	1.38	8.1	2.53
	5-Year Median	2.09	1.85	9.89	3.04
EV/EBITDA F12M	Current	13.13	9.53	32.76	13.21
	5-Year High	13.48	12.26	37.49	14.23
	5-Year Low	8.8	7.42	25.81	9.05
	5-Year Median	11.09	9.33	33.83	11.01

As of 08/06/2020

Industry Analysis Zacks Industry Rank: Bottom 49% (129 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
BrightView Holdings, Inc. (BV)	Neutral	3
Carriage Services, Inc. (CSV)	Neutral	2
1800 FLOWERS.COM, Inc. (FLWS)	Neutral	2
HR Block, Inc. (HRB)	Neutral	4
Matthews International Corporation (MATW)	Neutral	2
RentACenter, Inc. (RCII)	Neutral	3
SP Plus Corporation (SP)	Neutral	3
Hillenbrand Inc (HI)	Underperform	5

Industry Comparison Industry: Funeral Services				Industry Peers		
	SCI	X Industry	S&P 500	CSV	HI	MATW
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	3	-	-	2	5	2
VGM Score	B	-	-	B	B	A
Market Cap	8.20 B	1.54 B	23.20 B	405.80 M	2.39 B	693.92 M
# of Analysts	2	1	14	1	1	1
Dividend Yield	1.63%	2.15%	1.78%	1.32%	2.66%	3.78%
Value Score	B	-	-	B	B	A
Cash/Price	0.03	0.05	0.07	0.03	0.17	0.06
EV/EBITDA	12.79	13.48	13.21	12.02	14.17	15.89
PEG Ratio	2.42	1.75	2.94	0.97	NA	NA
Price/Book (P/B)	4.67	2.02	3.12	1.78	2.26	1.15
Price/Cash Flow (P/CF)	14.05	9.46	12.27	9.83	9.10	3.58
P/E (F1)	27.13	15.51	21.69	14.62	16.40	8.07
Price/Sales (P/S)	2.53	1.21	2.48	1.39	1.03	0.47
Earnings Yield	3.67%	6.47%	4.39%	6.84%	6.10%	12.39%
Debt/Equity	2.04	1.78	0.77	1.85	1.71	1.39
Cash Flow (\$/share)	3.31	3.41	6.94	2.31	3.52	6.20
Growth Score	C	-	-	C	B	A
Hist. EPS Growth (3-5 yrs)	13.30%	3.23%	10.46%	-6.68%	5.77%	0.68%
Proj. EPS Growth (F1/F0)	-10.00%	-5.81%	-6.80%	29.17%	-20.41%	-16.92%
Curr. Cash Flow Growth	2.68%	-0.63%	5.39%	-4.99%	3.57%	-3.95%
Hist. Cash Flow Growth (3-5 yrs)	4.63%	3.82%	8.55%	0.53%	3.00%	10.03%
Current Ratio	0.63	1.30	1.33	0.98	1.62	1.87
Debt/Capital	67.07%	63.96%	44.50%	64.87%	63.06%	58.20%
Net Margin	12.50%	0.30%	10.13%	1.83%	-1.23%	-11.11%
Return on Equity	20.42%	15.87%	14.39%	10.69%	17.93%	13.81%
Sales/Assets	0.24	0.45	0.51	0.27	0.62	0.68
Proj. Sales Growth (F1/F0)	-2.18%	-1.09%	-1.51%	12.72%	0.00%	-4.32%
Momentum Score	B	-	-	D	C	D
Daily Price Chg	2.06%	1.73%	-0.04%	0.94%	3.23%	1.39%
1 Week Price Chg	12.95%	11.66%	0.14%	16.98%	3.65%	10.37%
4 Week Price Chg	27.47%	27.57%	7.78%	32.44%	27.67%	22.83%
12 Week Price Chg	31.77%	45.28%	17.48%	58.79%	66.56%	14.05%
52 Week Price Chg	-0.81%	-0.27%	0.68%	0.27%	9.56%	-31.52%
20 Day Average Volume	1,285,044	344,391	2,057,775	155,998	414,558	274,223
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	7.42%
(F1) EPS Est 4 week change	32.00%	9.07%	1.36%	10.71%	0.00%	7.42%
(F1) EPS Est 12 week change	33.78%	15.71%	1.57%	24.00%	-15.22%	7.42%
(Q1) EPS Est Mthly Chg	35.09%	1.19%	0.54%	-6.06%	NA	1.19%

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	B
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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