

Service Corporation(SCI)

\$46.98 (As of 01/09/20)

Price Target (6-12 Months): **\$50.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/05/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: C

Growth: C

Momentum: D

Summary

Shares of Service Corporation have increased over the past year. Although the company posted lower-than-expected results for third-quarter 2019, its earnings grew year over year, driven by strength in funeral services and lower G&A expenses. Further, solid funeral margins, owing to an increase in funeral services performed, along with cost-cutting efforts contributed to the bottom line. Management remains optimistic about the fourth quarter. It expects to continue witnessing lower G&A expenses in the quarter. Also, the company's focus on acquisitions and building new funeral homes bodes well. However, rising interest expenses have been acting as a deterrent for a while. The use of alternative channels like e-commerce to buy funeral-related products is concerning.

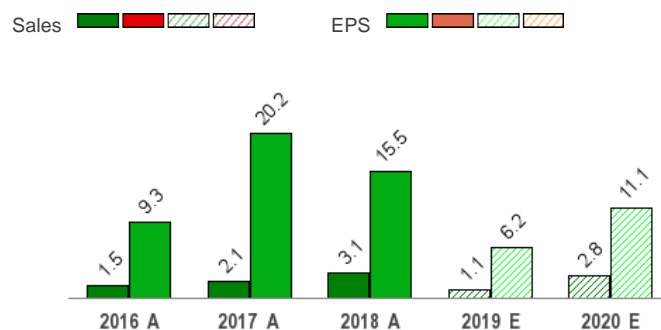
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$48.70 - \$38.92
20 Day Average Volume (sh)	704,463
Market Cap	\$8.6 B
YTD Price Change	2.1%
Beta	0.87
Dividend / Div Yld	\$0.72 / 1.5%
Industry	Funeral Services
Zacks Industry Rank	Top 43% (108 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-2.6%
Last Sales Surprise	-2.0%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/17/2020
Earnings ESP	0.0%
P/E TTM	25.4
P/E F1	22.3
PEG F1	2.0
P/S TTM	2.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	818 E	828 E	805 E	864 E	3,315 E
2019	798 A	813 A	769 A	844 E	3,224 E
2018	794 A	796 A	779 A	821 A	3,190 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.51 E	\$0.51 E	\$0.43 E	\$0.66 E	\$2.11 E
2019	\$0.47 A	\$0.47 A	\$0.37 A	\$0.60 E	\$1.90 E
2018	\$0.47 A	\$0.44 A	\$0.35 A	\$0.54 A	\$1.79 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 01/09/2020. The reports text is as of 01/10/2020.

Overview

Based in Texas and established in 1962, **Service Corporation International** is the largest deathcare products and services provider in North America. The company possesses a network of funeral service locations and cemeteries, spread across geographies.

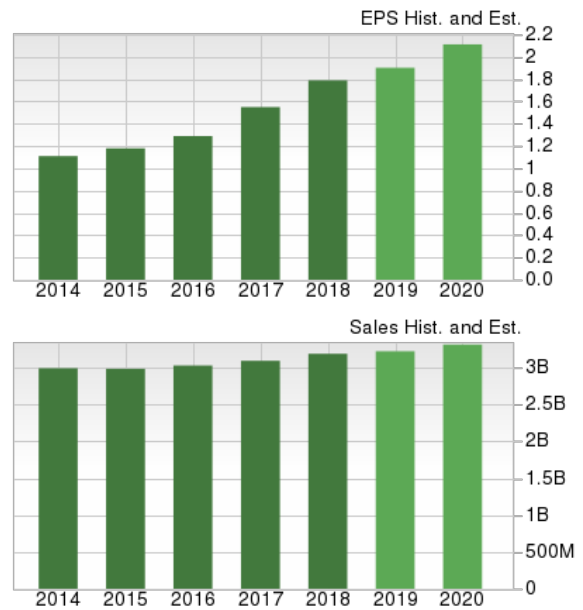
Service Corporation's funeral service and cemetery operations comprise funeral service locations, cemeteries, funeral service/cemetery combination locations, crematoria, and other related businesses. Notably, the company has the largest number of combination locations in North America. These varied businesses help the company cater to diverse customer needs. Also, Service Corporation sells cemetery property, and funeral and cemetery merchandise and services, both on an atneed and preneed basis.

Funeral service/cemetery combination locations are businesses, where a funeral service location is physically situated within or adjoining a cemetery owned by the company. Combination locations enable certain costs (related to facility, personnel, and equipment) to be shared between the funeral service location and cemetery locations.

Funeral service locations offer all professional services related to funerals and cremations, such as the use of funeral home facilities and motor vehicles, arranging and directing services, removal, preparation, embalming, cremations, memorialization, and catering. Funeral merchandise, including burial caskets and related accessories, stationery products, urns and other cremation receptacles, outer burial containers, flowers, online and video tributes, and other ancillary merchandise, is sold at funeral service locations.

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

As of Sep 30, 2019, the company operated 1,477 funeral service locations and 483 cemeteries across 44 states, eight provinces in Canada, the District of Columbia and Puerto Rico. Markedly, the cemeteries include 290 funeral service/cemetery combination locations.



Reasons To Buy:

▲ **Funeral Services Segment Robust:** Service Corporation posted third-quarter 2019 results, wherein earnings grew year over year, driven by strength in funeral services, and lower general and administrative expenses. Further, solid funeral margins, owing to an increase in funeral services performed, along with cost-cutting efforts contributed to the bottom line. Speaking of funeral services, revenues in the segment grew 1.3%, backed by improved preneed revenues along with higher core revenues and non-funeral revenues. Core revenues were up, owing to increased funeral services performed, which offset reduced average revenue per service conducted. Recognized preneed revenues improved 3.5% on high non-funeral home sales production, courtesy of growth in the number of contracts sold.

The company remains committed toward pursuing strategic buyouts and building new funeral homes to generate greater returns. Further, solid performance in the funeral service segment bodes well.

Management remains optimistic about the fourth quarter. It expects to continue witnessing lower G&A expenses in the quarter. That said, the company reiterated its bottom-line view for 2019. It continues to anticipate adjusted earnings of \$1.90-\$2, suggesting rise from the prior year's reported figure of \$1.79. We note that shares of the company have gained 13.6% in a year, compared with the industry's rise of 17.3%.

▲ **Focus on Acquisitions:** The company remains committed toward pursuing strategic buyouts for both its segments and building new funeral homes to generate greater returns. Service Corporation has a solid record of making and integrating prudent businesses. We note that buyouts are an integral part of the company's capital investment ventures targeted toward growth. It deployed \$50-\$100 million for 2019, with \$32 million already spent on acquisitions year to date. For the fourth quarter, management remains optimistic about its expansion plans. It invested additional \$44.6 million in building cemeteries and expanding funeral homes.

In 2018, the company deployed approximately \$200 million towards acquisitions. Some notable acquisitions made by the company in the past includes 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. The company has a targeted dividend payout ratio of 30-40% of earnings. Notably, in Feb 2019, the company hiked quarterly cash dividend rate by 6%, taking it from 17 cents per share to 18 cents.

Moving to share buybacks, management has recently increased its buyback authorization by nearly \$246 million, post which it has share repurchase capacity of \$400 million. During the third quarter, Service Corporation returned \$55.5 million to its shareholders via dividends and share buybacks, and invested \$44.6 million in land for new cemeteries and funeral homes.

Reasons To Sell:

▼ **High Costs:** Service Corporation is witnessing escalated interest expense for a while now. In the third quarter of 2019, interest costs rose 0.3 million to \$46.7 million. Prior to this, the metric rose \$2.8 million and \$3.8 million to \$47.3 million \$47.4 million in the second and first quarters, respectively. Moreover, interest costs rose by \$3.4 million and \$3.7 million during the fourth and third quarters of 2018, respectively. We believe that persistence of high costs may weigh on the company's bottom line in the near term.

The company has been witnessing rising interest costs, which is a concern. Also, continued rise in cremations poses threats to the company.

▼ **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.

▼ **Increased Cremations:** The company has been witnessing a continued rising trend in the number of cremations, as another option to the traditional funeral service. Well, the company's average revenue from cremations with service is usually lower compared to that for traditional burials. Continuance of such trends remains a threat to the company's overall performance.

Last Earnings Report

Service Corporation Q3 Earnings Miss, Revenues Down Y/Y

Service Corporation posted lower-than-expected results for third-quarter 2019. Although the company's earnings grew on a year-over-year basis, revenues declined. Results were affected by sluggish preneed cemetery sales production in two West Coast markets in Asia.

However, solid funeral revenues and margins, owing to an increase in funeral services performed, along with cost-cutting efforts contributed to the third-quarter results to some extent. Further, management reiterated its bottom-line view for 2019. The company continues to anticipate adjusted earnings of \$1.90-\$2, which is up from the last year's reported figure of \$1.79.

Quarter Ending **09/2019**

Report Date	Oct 30, 2019
Sales Surprise	-1.96%
EPS Surprise	-2.63%
Quarterly EPS	0.37
Annual EPS (TTM)	1.85

Q3 in Detail

Service Corporation reported adjusted earnings of 37 cents per share, missing the Zacks Consensus Estimate by a penny. However, the bottom line improved 5.7% from the year-ago quarter, driven by strength in funeral services, and lower general and administrative expenses. However, soft cemetery revenues hurt the bottom line to some extent.

Adjusted effective tax rate was 18.5% in the third quarter of 2019 compared with 17.6% in the same period last year.

Total revenues of \$769.2 million edged down 1.2% from \$778.8 million in the year-ago quarter, due to soft performance in cemetery revenues. Moreover, the figure lagged the consensus mark of \$785 million.

General and administrative costs dipped 28.4% to reach \$29.4 million. The decline resulted from higher costs incurred in the prior-year quarter due to its long-term incentive compensation plan.

Meanwhile, the company's interest costs inched up 0.6% to \$46.7 million in the reported quarter.

Segment Discussion

Comparable Funeral revenues grew 1.3%, backed by improved preneed revenues along with higher core revenues and non-funeral revenues. Core revenues were up, owing to increased funeral services performed, which offset the reduced average revenue per service conducted. Recognized preneed revenues improved 3.5% on high non-funeral home sales production, courtesy of growth in the number of contracts sold.

Comparable preneed funeral sales production rose 1.8%, driven by sales growth in non-funeral home channel and increase in core funeral locations.

Comparable funeral operating profit advanced 8.4% at \$73.9 million, driven by cost-effective initiatives. Also, the operating margin expanded 110 basis points (bps) to 16.5%.

Comparable Cemetery revenues fell 5.8% year over year on soft recognized preneed property revenues and other revenues. These downsides were partly offset by growth in atneed revenues, and recognized preneed merchandise and service revenues. Comparable preneed cemetery sales production dipped 2.3%.

Comparable cemetery operating profit declined around 12.2% to \$85.3 million and the respective margin contracted 210 bps to 28%. The decline can be attributable to lower recognized preneed property revenues, slightly offset by cost-reduction plans.

Other Financial Details

The company ended the quarter with cash and cash equivalents of \$194.7 million, long-term debt of \$3,466.8 million, and total equity of approximately \$1,775.5 million.

Net cash from operating activities (excluding special items) amounted to \$209.3 million in the quarter compared with \$136.9 million in the prior-year period, driven by improved performance in atneed operations, higher preneed installment collections and an increase in working capital.

During the third quarter, Service Corporation returned \$55.5 million to its shareholders via dividends and share buybacks and invested \$44.6 million in land for new cemeteries and building new funeral homes.

Further, the company incurred capital expenditure of \$64.5 million in the third quarter of 2019.

Outlook

The company now projects net cash from operating activities (excluding special items) of \$575-\$615 million.

It still plans to allocate about \$195 million toward capital enhancements at existing facilities and cemetery development.

Recent News

Service Corporation Approves Dividend – Aug 14, 2019

Service Corporation has approved a quarterly cash dividend of 18 cents per share, which is payable on Sep 30, 2019 to shareholders of record as on Sep 13. Also, the company's board raised the authorized level of repurchases of its common stock by nearly \$246 million. Prior to this, it had roughly \$154 million remaining under the existing program. Post this announcement, the company has \$400 million of current share repurchase authority effective from Aug 14.

Valuation

Service Corporation's shares are up 13.6% in the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are up 17.3% and 20.1% over the past year.

The S&P 500 index is up 27.1% in the past year.

The stock is currently trading at 22.18X forward 12-month earnings, which compares to 17.57X for the Zacks sub-industry, 19.75X for the Zacks sector and 18.81X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.12X and as low as 16.94X, with a 5-year median of 21.51X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$50 price target reflects 23.61X 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	22.18	17.57	19.75	18.81
	5-Year High	25.12	27.39	22.39	19.34
	5-Year Low	16.94	14.94	16.65	15.17
	5-Year Median	21.51	19.46	19.75	17.44
P/S F12M	Current	2.59	1.91	9.83	3.49
	5-Year High	2.67	1.99	11.03	3.49
	5-Year Low	1.37	1.43	8.02	2.54
	5-Year Median	2.01	1.73	9.78	3
EV/EBITDA F12M	Current	12.33	8.08	34.12	12.66
	5-Year High	12.9	14.54	36.97	12.66
	5-Year Low	8.92	7.13	29.14	9.08
	5-Year Median	10.91	8.75	33.27	10.78

As of 01/09/2020

Industry Analysis Zacks Industry Rank: Top 43% (108 out of 254)



Top Peers

H&R Block, Inc. (HRB)	Outperform
BrightView Holdings, Inc. (BV)	Neutral
Care.com, Inc. (CRCM)	Neutral
Carriage Services, Inc. (CSV)	Neutral
1-800 FLOWERS.COM, Inc. (FLWS)	Neutral
Hillenbrand Inc (HI)	Neutral
Rent-A-Center, Inc. (RCII)	Neutral
Matthews International Corporation (MATW)	Underperform

Industry Comparison Industry: Funeral Services				Industry Peers		
	SCI Neutral	X Industry	S&P 500	CSV Neutral	HI Neutral	MATW Underperform
VGM Score	C	-	-	A	A	B
Market Cap	8.59 B	1.62 B	23.94 B	446.73 M	2.08 B	1.16 B
# of Analysts	3	1	13	1	2	2
Dividend Yield	1.53%	1.90%	1.78%	1.20%	2.57%	2.26%
Value Score	C	-	-	A	A	B
Cash/Price	0.02	0.03	0.04	0.01	0.19	0.03
EV/EBITDA	13.51	13.31	13.97	13.11	8.53	21.64
PEG Ratio	2.00	1.50	2.03	1.01	NA	NA
Price/Book (P/B)	4.84	2.35	3.33	1.99	2.70	1.63
Price/Cash Flow (P/CF)	14.41	10.07	13.73	10.71	9.42	5.99
P/E (F1)	22.39	13.91	18.79	15.20	12.62	10.91
Price/Sales (P/S)	2.68	1.41	2.64	1.66	1.15	0.76
Earnings Yield	4.49%	7.26%	5.32%	6.58%	7.94%	9.15%
Debt/Equity	1.95	1.46	0.72	1.68	0.80	1.25
Cash Flow (\$/share)	3.26	3.39	6.94	2.34	3.52	6.20
Growth Score	C	-	-	B	B	C
Hist. EPS Growth (3-5 yrs)	13.19%	4.92%	10.56%	-5.51%	3.95%	5.88%
Proj. EPS Growth (F1/F0)	11.03%	9.98%	7.49%	22.22%	7.14%	2.87%
Curr. Cash Flow Growth	6.60%	-0.19%	14.83%	-7.76%	3.57%	-3.95%
Hist. Cash Flow Growth (3-5 yrs)	7.66%	7.30%	9.00%	6.93%	3.00%	10.03%
Current Ratio	0.63	1.28	1.23	0.82	1.74	2.09
Debt/Capital	66.13%	59.09%	42.99%	62.64%	44.59%	55.53%
Net Margin	12.98%	5.09%	11.08%	3.45%	6.72%	-2.47%
Return on Equity	19.90%	16.36%	17.16%	9.72%	20.10%	12.82%
Sales/Assets	0.24	0.48	0.55	0.29	0.92	0.67
Proj. Sales Growth (F1/F0)	2.81%	2.28%	4.20%	16.54%	0.00%	1.75%
Momentum Score	D	-	-	D	B	B
Daily Price Chg	0.75%	-0.04%	0.53%	-0.79%	0.00%	-0.08%
1 Week Price Chg	0.28%	0.58%	-0.30%	-0.97%	0.87%	2.31%
4 Week Price Chg	3.48%	-1.26%	1.92%	-9.20%	-1.13%	-1.38%
12 Week Price Chg	0.82%	7.44%	6.54%	16.70%	10.51%	4.38%
52 Week Price Chg	12.45%	-1.02%	22.58%	50.72%	-16.51%	-14.48%
20 Day Average Volume	704,463	343,102	1,580,816	81,336	573,649	112,554
(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	-0.78%	-0.77%	-0.50%	4.43%	-0.76%	-7.47%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	NA	NA	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	C
Momentum Score	D
VGM Score	C

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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