

Service Corporation(SCI)

\$48.59 (As of 02/27/20)

Price Target (6-12 Months): **\$52.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/05/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:C

Value: D

Growth: B

Momentum: B

Summary

Shares of Service Corporation have risen and outpaced the industry in the past three months. Although the company's adjusted earnings came in line with estimates for fourth-quarter 2019, the metric grew year over year, driven by strength in funeral services revenues and lower G&A expenses. Also, sales beat the consensus mark and improved year over year on strong growth in both funeral and cemetery segments. Encouragingly, management provided an upbeat view for 2020. Apart from these, the company's focus on acquisitions and building new funeral homes bodes well. However, rising expense woes are likely to persist in 2020 due to building funeral homes and cemetery inventory development. Also, intense competition and the use of alternative channels like e-commerce to buy funeral-related products are concerns.

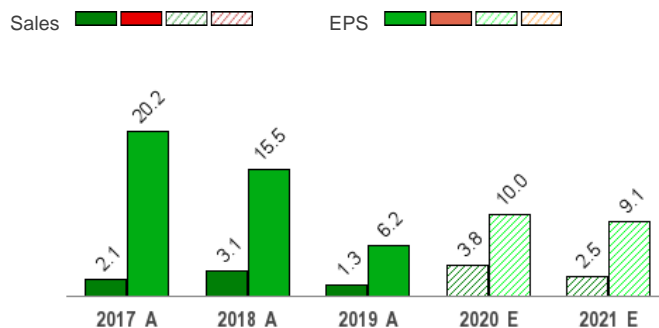
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$52.74 - \$38.92
20 Day Average Volume (sh)	913,089
Market Cap	\$8.8 B
YTD Price Change	5.6%
Beta	0.87
Dividend / Div Yld	\$0.76 / 1.5%
Industry	Funeral Services
Zacks Industry Rank	Bottom 5% (242 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.0%
Last Sales Surprise	0.8%
EPS F1 Est- 4 week change	-1.3%
Expected Report Date	04/22/2020
Earnings ESP	1.3%
P/E TTM	25.4
P/E F1	23.3
PEG F1	2.1
P/S TTM	2.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	857 E	869 E	851 E	913 E	3,440 E
2020	827 E	839 E	814 E	876 E	3,355 E
2019	798 A	813 A	769 A	851 A	3,231 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.57 E	\$0.55 E	\$0.47 E	\$0.70 E	\$2.28 E
2020	\$0.51 E	\$0.52 E	\$0.42 E	\$0.65 E	\$2.09 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.

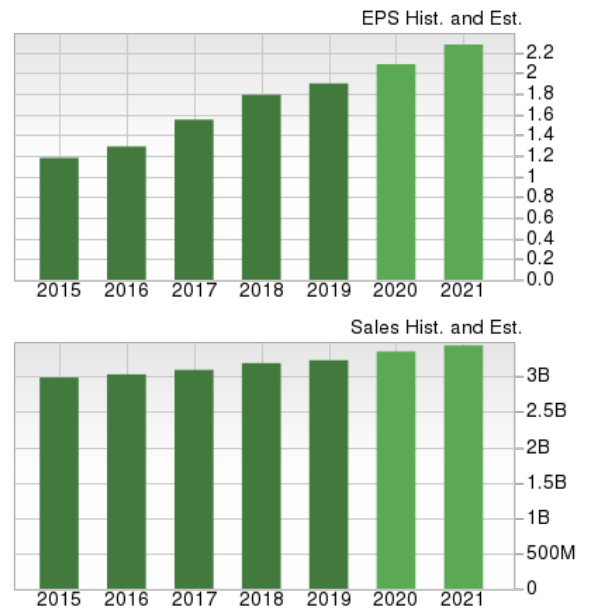
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/27/2020. The reports text is as of 02/28/2020.

Overview

Known for its transcontinental brand namely Dignity Memorial, Service Corporation International has been strengthening its funeral and cemetery businesses, which 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 benefit from the aging Baby Boomer generation. To this end, its funeral service locations, cemeteries, funeral service/cemetery combination locations, crematoria and other related businesses spread across geographies are noteworthy. Further, the company's active buyout efforts, including 15 funeral homes and seven cemeteries in June 2018, have been accretive.

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 Dec 31, 2019, the company 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:

▲ **Funeral Services Segment Robust:** Service Corporation posted fourth-quarter 2019 results, wherein earnings grew year over year, driven by strength in funeral services, and lower general and administrative expenses. Speaking of funeral services, revenues in the segment grew 5.1%, backed by improved preneed revenues along with higher core revenues. Core revenues were up, owing to increased funeral services performed and higher average revenue per service conducted. Recognized pre-need revenues improved 29.7% on high non-funeral home sales production, courtesy of growth in the number of contracts sold and a hike in average revenue per contract sold. Going into 2020, management expects core funeral revenue rise of 1-2% and total preneed funeral sales production increase of 3-5%. Moreover, funeral services performed and sales averages are anticipated to be flat to marginally up in 2020. We note that shares of the company have gained 10.4% in the past three months compared with the industry's growth of 0.1%.

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.

▲ **Improved Cemetery Segment & Upbeat View Bodes Well:** After delivering sluggish performance in the third quarter, the company's cemetery segment came back to growth in the fourth quarter of 2019. Notably, comparable Cemetery revenues inched up 0.5% year over year on solid recognized pre-need property revenues. Moreover, comparable pre-need cemetery sales production rose 5.2%. Going into 2020, management remains optimistic about the segment. In this regard, it forecasts sales productions and cemetery operating revenues to grow in mid-single digits along with positive cemetery operating profit and margins. In fact, margins in the segment have been anticipated to be more than 30%.

▲ **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 \$107 million for 2019, with \$56 million already spent on acquisitions, and \$51 million was invested in building two cemeteries and new funeral homes. These investments are touted to be accretive to the company in the near term. Going ahead, it envisions deploying \$100-\$125 million in acquisitions and other growth initiatives such as building funeral homes. Out of this, \$75 million is projected to be reserved for buyout purposes.

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 fourth quarter, Service Corporation returned \$110.2 million to its shareholders via dividends and share buybacks, and invested \$48.2 million in land for building funeral homes and buyout purposes. Management expects solid cash flow in 2020. In fact, net cash from operating activities (excluding special items) is guided to be \$590-\$640 million.

Reasons To Sell:

- ▼ **High Costs:** Although Service Corporation witnessed reduced interest expenses for the fourth quarter of 2019, the metric rose \$0.3 million, \$2.8 million and \$3.8 million to \$46.7 million, \$47.3 million and \$47.4 million in the third, 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. In fact, management envisions a slight increase in expenses, driven by cemetery inventory development and the construction of funeral homes in 2020.
- ▼ **Stock Looks Overvalued:** Considering 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 22.95, which is above its median level of 22.07 but below the high level of 24.86 scaled in a year. Meanwhile, the trailing 12-month P/E ratio for the industry is currently pegged at 17.01.
- ▼ **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.

High costs is likely to persist due to building of funeral homes and cemetery inventory development. Also, continued rise in cremations poses threats to the company.

Last Earnings Report

Service Corporation Q4 Earnings In Line, Increase Y/Y

Service Corporation posted fourth-quarter 2019 results, wherein earnings were in line, while sales surpassed the Zacks Consensus Estimate. Further, both metrics improved year over year. Results were driven by solid performance in the funeral segment, partly offset by unfavorable timing of revenue recognition related to the cemetery sales production.

Q4 in Detail

Service Corporation reported adjusted earnings of 60 cents per share, which were in line with the Zacks Consensus Estimate. Further, the bottom line improved 11.1% from the year-ago quarter, driven by strength in funeral services, and lower general and administrative expenses. However, soft cemetery revenues and an elevated tax hurt the bottom line to some extent.

Total revenues of \$850.8 million moved up 3.7% from \$820.8 million in the year-ago quarter, backed by solid funeral revenues. Moreover, the figure beat the consensus mark of \$844 million.

General and administrative costs dipped 34.4% to \$25 million. The decline resulted from reduced costs in the quarter due to its long-term and short-term incentive compensation plan.

Additionally, the company's interest costs declined 5.5% to \$44.5 million in the reported quarter.

Segment Discussion

Comparable Funeral revenues grew 5.1%, backed by improved preneed revenues along with higher core revenues. Core revenues were up, owing to increased funeral services performed and higher average revenue per service conducted. Recognized pre-need revenues improved 29.7% on high non-funeral home sales production, courtesy of growth in the number of contracts sold and a hike in average revenue per contract sold.

Comparable pre-need funeral sales production rose 12.1%, driven by rise in pre-need production in non-funeral home channel and an increase in core funeral locations.

Comparable funeral gross profit advanced 10% to \$100.8 million, driven by sales growth, partly offset by rise in selling compensation, owing to higher pre-need funeral sales production. Also, the gross margin expanded 100 basis points (bps) to 21.1%.

Comparable Cemetery revenues inched up 0.5% year over year on solid recognized pre-need property revenues. This was partly offset by a decline in recognized pre-need merchandise and service revenues. Comparable pre-need cemetery sales production rose 5.2%.

Comparable cemetery gross profit declined 3% to \$114.6 million and the respective margin contracted 120 bps to 32.5%. The decline can be attributable to flat cemetery sales as well as cost inflation.

Other Financial Details

The company ended the quarter with cash and cash equivalents of \$186.3 million, long-term debt of \$3,513.5 million, and total equity of \$1,823.3 million.

Net cash provided by operating activities (excluding special items) amounted to \$156.6 million in the quarter compared with \$163.5 million in the prior-year period.

During the fourth quarter, Service Corporation returned \$110.2 million to its shareholders via dividends and share buybacks, and invested \$48.2 million in land for building funeral homes and buyout purposes.

Further, it incurred capital expenditure of \$62.8 million in the fourth quarter of 2019.

Outlook

For 2020, the company projects net cash from operating activities (excluding special items) of \$590-\$640 million. Adjusted earnings are anticipated to be \$1.96-\$2.16 per share, whereas it reported \$1.90 in the last year. However, rise in effective tax rate is likely to affect the bottom line to the tune of 5 cents in 2020.

Moving on, core funeral revenues are estimated to rise 1-2% and total preneed funeral sales production is likely to increase 3-5%. Moreover, funeral services performed and sales averages are anticipated to be flat to marginally up during 2020. Speaking of the cemetery segment, the company forecasts sales productions and cemetery operating revenues to grow in mid-single digits along with positive cemetery operating profit and margins. In fact, margins in the segment have been anticipated to be more than 30%.

Service Corporation plans to allocate \$230 million toward capital enhancements at existing facilities and cemetery development.

Quarter Ending **12/2019**

Report Date	Feb 17, 2020
Sales Surprise	0.77%
EPS Surprise	0.00%
Quarterly EPS	0.60
Annual EPS (TTM)	1.91

Recent News

Service Corporation Hikes Dividend – Feb 20, 2020

Service Corporation has approved a raise of 6% on the quarterly cash dividend of 18 cents per share. This will be payable on Mar 31, 2020 to shareholders of record as on Mar 13.

Valuation

Service Corporation's shares are up 5.5% in the year-to-date period and 16.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are down 4% and 8.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 2.7%, while the sector gained 0.9%.

The S&P 500 index is down 7.6% in the year-to-date period and up 5.4% in the past year.

The stock is currently trading at 22.95X forward 12-month earnings, which compares to 17.01X for the Zacks sub-industry, 17.92X for the Zacks sector and 17.03X 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 21.64X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$52 price target reflects 24.56X 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	22.95	17.01	17.92	17.03
	5-Year High	25.12	23.78	22.38	19.34
	5-Year Low	16.94	15.74	16.66	15.18
	5-Year Median	21.64	18.16	19.68	17.44
P/S F12M	Current	2.61	1.82	9.14	3.14
	5-Year High	2.85	2.19	11.13	3.43
	5-Year Low	1.37	1.49	8.09	2.54
	5-Year Median	2.03	1.86	9.88	3
EV/EBITDA F12M	Current	13.56	10.71	34.39	13.54
	5-Year High	13.56	12.27	37.23	13.72
	5-Year Low	8.92	7.41	29.38	9.08
	5-Year Median	11.02	9.24	33.59	10.81

As of 02/27/2020

Industry Analysis Zacks Industry Rank: Bottom 5% (242 out of 254)



Top Peers

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

Industry Comparison Industry: Funeral Services				Industry Peers		
	SCI Neutral	X Industry	S&P 500	CSV Neutral	HI Neutral	MATW Neutral
VGM Score	C	-	-	B	D	C
Market Cap	8.78 B	1.35 B	21.35 B	371.02 M	1.78 B	922.12 M
# of Analysts	3	1	13	1	2	2
Dividend Yield	1.48%	2.17%	2.02%	1.44%	3.56%	2.85%
Value Score	D	-	-	B	C	C
Cash/Price	0.02	0.03	0.04	0.01	0.07	0.04
EV/EBITDA	13.41	13.39	12.70	11.90	13.37	19.47
PEG Ratio	2.01	1.48	1.84	0.87	NA	NA
Price/Book (P/B)	4.87	1.48	2.92	1.65	1.31	1.29
Price/Cash Flow (P/CF)	14.67	7.84	11.89	8.90	6.79	4.75
P/E (F1)	22.54	11.29	16.90	13.02	9.55	8.68
Price/Sales (P/S)	2.72	1.13	2.39	1.35	0.91	0.60
Earnings Yield	4.30%	9.08%	5.90%	7.68%	10.47%	11.50%
Debt/Equity	1.93	1.69	0.70	1.68	1.71	1.32
Cash Flow (\$/share)	3.31	3.41	6.94	2.34	3.52	6.20
Growth Score	B	-	-	C	D	D
Hist. EPS Growth (3-5 yrs)	13.28%	4.78%	10.85%	-6.42%	5.10%	4.46%
Proj. EPS Growth (F1/F0)	9.83%	6.89%	6.79%	33.33%	2.04%	2.57%
Curr. Cash Flow Growth	2.68%	-0.63%	5.92%	-7.76%	3.57%	-3.95%
Hist. Cash Flow Growth (3-5 yrs)	4.63%	5.78%	8.38%	6.93%	3.00%	10.03%
Current Ratio	0.67	1.11	1.23	0.82	1.39	2.10
Debt/Capital	65.84%	62.89%	42.53%	62.64%	63.15%	56.81%
Net Margin	11.44%	4.94%	11.57%	5.30%	4.58%	-3.37%
Return on Equity	20.05%	16.16%	16.80%	9.98%	19.15%	13.16%
Sales/Assets	0.24	0.48	0.54	0.29	0.75	0.67
Proj. Sales Growth (F1/F0)	3.85%	2.80%	4.07%	15.47%	0.00%	1.75%
Momentum Score	B	-	-	F	C	A
Daily Price Chg	-3.53%	-1.96%	-3.99%	-1.28%	-2.21%	-1.70%
1 Week Price Chg	5.14%	1.27%	-0.94%	-10.79%	3.40%	-0.87%
4 Week Price Chg	0.58%	-16.77%	-9.83%	-13.75%	-19.79%	-22.35%
12 Week Price Chg	10.89%	-22.18%	-6.79%	-20.89%	-25.20%	-23.47%
52 Week Price Chg	17.54%	-13.38%	2.79%	-0.86%	-46.11%	-25.90%
20 Day Average Volume	913,089	524,073	2,169,477	110,480	907,289	140,857
(F1) EPS Est 1 week change	0.00%	-0.37%	0.00%	-3.03%	0.00%	-0.73%
(F1) EPS Est 4 week change	-1.26%	-2.15%	-0.09%	-3.03%	-8.57%	-0.29%
(F1) EPS Est 12 week change	-1.26%	-0.78%	-0.24%	0.00%	-8.57%	-0.29%
(Q1) EPS Est Mthly Chg	1.65%	-4.87%	-0.72%	NA	NA	-11.39%

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	B
Momentum Score	B
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.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.