

ServiceMaster (SERV)

\$20.36 (As of 03/18/20)

Price Target (6-12 Months): **\$17.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 03/17/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:F

Value: F

Growth: D

Momentum: B

Summary

High cost of termite damage claims related to Formosan termite activity in the Mobile, Alabama is a concern. ServiceMaster expects cost increase in 2020, which is likely to keep its bottom line under pressure, thereby weighing on the stock that has underperformed its industry in the past year. High debt and seasonality are other concerns for the company. On the flip side, ServiceMaster's size and scale provide it competitive advantage in terms of purchasing power, operating and marketing efficiencies, and route density. The company enjoys brand awareness and a reputation of high-quality customer service. Its capital-light business model is characterized by strong Adjusted EBITDA margins and limited capital expenditure requirements. This model enjoys operating leverage from route density and fixed investments in infrastructure and technology.

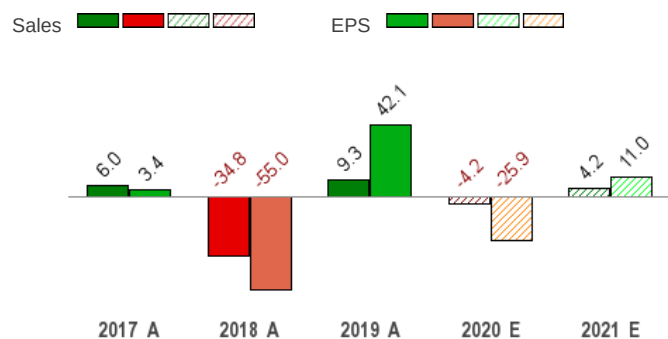
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$58.78 - \$17.63
20 Day Average Volume (sh)	2,490,987
Market Cap	\$2.8 B
YTD Price Change	-47.3%
Beta	0.34
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Building Products - Maintenance Service
Zacks Industry Rank	Bottom 6% (239 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	15.8%
Last Sales Surprise	-0.1%
EPS F1 Est- 4 week change	-29.3%
Expected Report Date	05/05/2020
Earnings ESP	0.0%
P/E TTM	15.0
P/E F1	20.4
PEG F1	1.2
P/S TTM	1.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	481 E	572 E	546 E	487 E	2,073 E
2020	462 E	546 E	517 E	465 E	1,989 E
2019	482 A	560 A	528 A	507 A	2,077 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.22 E	\$0.36 E	\$0.25 E	\$0.20 E	\$1.11 E
2020	\$0.22 E	\$0.39 E	\$0.21 E	\$0.15 E	\$1.00 E
2019	\$0.33 A	\$0.50 A	\$0.31 A	\$0.22 A	\$1.35 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 03/18/2020. The reports text is as of 03/19/2020.

Overview

Founded in 1929 and headquartered in Memphis, Tennessee, ServiceMaster is a leading provider of essential services to residential and commercial customers in the termite, pest control, cleaning and restoration markets. The company operates through an extensive network of more than 8,000 company-owned locations and franchise and license agreements.

The company's revenue streams are diversified across customers and geographies, allowing it to mitigate risks in any particular customer segment and geography. ServiceMaster's capital-light business model is characterized by strong Adjusted EBITDA margins and limited capital expenditure requirements. This model enjoys operating leverage from route density and fixed investments in infrastructure and technology.

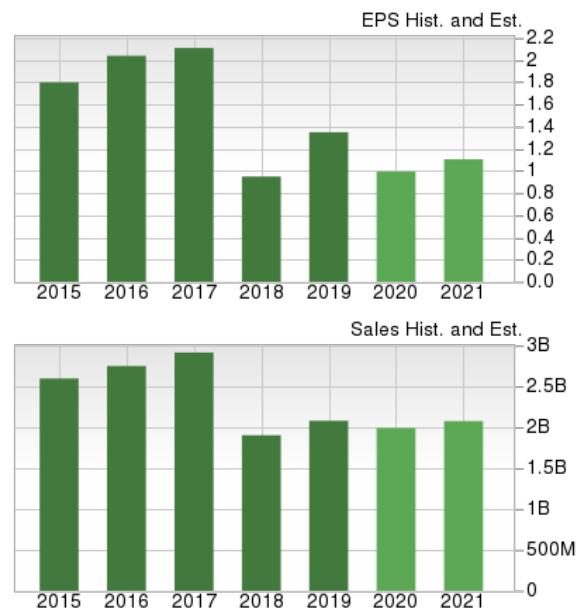
ServiceMaster operates two reportable segments, **Terminix** and **ServiceMaster Brands**.

The Terminix segment provides termite and pest control services encompassing termite remediation, annual termite inspection and prevention treatments with damage claim guarantees, periodic pest control services, insulation services, mosquito control, crawlspace encapsulation, and wildlife exclusion.

The ServiceMaster Brands segment provides restoration, emergency response, commercial and residential cleaning, and information technology services. The segment operates under ServiceMaster, Terminix, Copesan, ServiceMaster Restore, ServiceMaster Clean, Merry Maids, Furniture Medic, and AmeriSpec trademarks and trade names.

ServiceMaster consists of an employee base of around 10,700 company associates and 34,000 employees of licensed franchisors. In 2019, the company had revenues, net income and Adjusted EBITDA of \$2,077 million, \$128 million and \$417 million, respectively. Terminix was the company's largest segment representing 87% of revenues, while ServiceMaster Brand represented the rest 12%.

ServiceMaster markets its services on a national and local level through the internet, direct mail, print advertisements, television and radio advertising, marketing partnerships, telemarketing, social media channels and national sales teams. With nationwide presence, its segments are large, growing and highly fragmented.



Reasons To Sell:

- ▼ ServiceMaster has a highly leveraged balance sheet. As of Dec 31, 2019, long-term debt was \$1.7 billion while cash and cash equivalents were \$280 million. Such a cash position implies that ServiceMaster 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.
- ▼ ServiceMaster's business is affected by weather conditions. Cooler temperatures and droughts obstruct development of termite swarms thus reducing demand for the company's termite control services. Pest control services and restoration services are also seasonal in nature. Seasonality causes considerable fluctuations in revenues and Adjusted EBITDA.
- ▼ Cost of termite damage claims related to Formosan termite activity in the Mobile, Alabama area has increased over the past few years. The company has also witnessed increase in the number of termite damage claims that involves litigation. These two trends have increased ServiceMaster's termite damage claim costs as a percentage of termite revenue between 7% and 8%. The company expects additional cost increase in 2020, which is likely to keep the bottom line under pressure, thereby weighing on the stock that has decreased 57.2% in the past year compared with 26.3% decline of the industry it belongs to.

High debt, seasonality of business and high cost of termite damage claims are risks for ServiceMaster.

Risks

- ServiceMaster's size and scale provide it competitive advantage in terms of purchasing power, operating and marketing efficiencies, and route density. The company enjoys brand awareness and a reputation of high-quality customer service. With nationwide presence, its segments are large, growing and highly fragmented. ServiceMaster is focused on improving its business through investments sales, marketing and advertising, as well as brand awareness and market penetration initiatives.
 - The company's capital-light business model is characterized by strong Adjusted EBITDA margins and limited capital expenditure requirements. This model enjoys operating leverage from route density and fixed investments in infrastructure and technology. This helps generate productivity and expand margins through a number of initiatives such as metricdriven continuous improvement in customer care centers, application of consistent process guidelines at the branch level, leveraging size and scale to improve the sourcing of labor and materials, and deploying shared services models. The company has also deployed mobility solutions and routing and scheduling systems across many of its businesses in order to enhance overall efficiency and reduce operating costs.
 - The company's revenue streams are diversified across customers and geographies, allowing it to mitigate risks in any particular customer segment and geography. Prudent investments and operational execution keep its revenues and adjusted EBITDA in a good shape. Consolidated revenue and Adjusted EBITDA grew at compound annual growth rates (CAGR) of 5.5% and 1.8%, respectively, from 2015 to 2019.
 - Acquisition is an integral part of ServiceMaster's growth strategy. They have helped the company enhance offerings, expand geographic footprint and increase talent levels. From 2014 to 2019, the company completed around 114 acquisitions, out of which 39 were in 2019.
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Last Earnings Report

ServiceMaster Beats on Q4 Earnings, Revenues Lag Estimates

ServiceMaster Global Holdings reported mixed fourth-quarter 2019 results wherein earnings beat the Zacks Consensus Estimate but revenues lagged the same.

Adjusted EPS of 22 cents came above the consensus mark as well as the year-ago figure by 16%. Lower year-over-year tax expense drove the bottom line.

Revenues of \$507 million marginally missed the consensus mark but increased 11% year over year. The top line benefited from acquisitions, progress on commercial national account and health care cleaning and disinfection.

Other Quarterly Numbers

Terminix revenues of \$423 million increased 7% year over year. ServiceMaster Brands revenues increased 8% year over year to \$66 million.

Adjusted EBITDA of \$80 million was roughly flat year over year. Adjusted EBITDA margin of 15.7% declined 190 basis points year over year.

The company exited the quarter with cash and cash equivalent balance of \$280 million compared with \$140 million at the end of prior quarter. Long-term debt was \$1.7 billion compared with \$1.4 billion at the end of prior quarter.

The company generated \$32 million of cash from operating activities. Free cash flow came in at \$25 million. It repurchased \$14 million of shares in the quarter.

2020 Outlook

ServiceMaster expects 2020 revenues in the range of \$1.98-\$2 billion. Organic revenue growth at Terminix is expected to lie between 3% and 4%. Adjusted EBITDA is expected between \$320 million and \$335 million.

Quarter Ending **12/2019**

Report Date	Feb 27, 2020
Sales Surprise	-0.14%
EPS Surprise	15.79%
Quarterly EPS	0.22
Annual EPS (TTM)	1.36

Recent News

On Dec 4, 2019, ServiceMaster announced joining of Kim Scott as president of Terminix Residential.

Valuation

ServiceMaster shares are down 57.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Business Services sector are down 26.3% and 18.8%, respectively, over the past year.

The S&P 500 index is down 11.6% in the same time frame.

The stock is currently trading at 1.38X forward 12-month price-to-earnings, which compares to 2.63X for the Zacks sub-industry, 3.03X for the Zacks sector and 2.71X for the S&P 500 index.

Over the past five years, the stock has traded as high as 3.75X and as low as 1.38X, with a 5-year median of 2.04X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$17.00 price target reflects 1.15X price-to-earnings.

The table below shows summary valuation data for SERV

Valuation Multiples - SERV					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	1.38	2.63	3.03	2.71
	5-Year Hig	3.75	4.77	3.94	3.43
	5-Year Lov	1.38	2.4	3.03	2.54
	5-Year Me	2.04	3.09	3.57	3
P/B TTM	Current	1.19	5.56	3.35	3.4
	5-Year Hig	13.73	12.53	6.68	4.55
	5-Year Lov	1.19	5.56	3.22	2.85
	5-Year Me	7.36	10.24	5.19	3.63
EV/EBITDA TTM	Current	10.66	23.04	9.25	8.87
	5-Year Hig	29.48	32.47	13.24	12.88
	5-Year Lov	10.41	17.04	8.52	8.31
	5-Year Me	14.32	23.28	10.46	10.78

As of 03/18/2020

Industry Analysis Zacks Industry Rank: Bottom 6% (239 out of 253)



Top Peers

ABM Industries Incorporated (ABM)	Neutral
Church & Dwight Co., Inc. (CHD)	Neutral
Ecolab Inc. (ECL)	Neutral
EMCOR Group, Inc. (EME)	Neutral
Johnson Controls International plc (JCI)	Neutral
Limbach Holdings, Inc. (LMB)	Neutral
Rollins, Inc. (ROL)	Neutral
Team, Inc. (TISI)	Underperform

Industry Comparison Industry: Building Products - Maintenance Service				Industry Peers		
	SERV Underperform	X Industry	S&P 500	LMB Neutral	ROL Neutral	TISI Underperform
VGM Score	F	-	-	-	C	A
Market Cap	2.76 B	1.65 B	16.02 B	28.45 M	12.13 B	204.78 M
# of Analysts	8	3	13	0	3	1
Dividend Yield	0.00%	0.00%	2.66%	0.00%	1.30%	0.00%
Value Score	F	-	-	-	F	B
Cash/Price	0.07	0.04	0.06	0.03	0.01	0.04
EV/EBITDA	12.16	18.78	10.21	18.78	36.16	67.16
PEG Ratio	1.21	1.20	1.46	0.31	NA	NA
Price/Book (P/B)	1.19	1.06	2.18	0.63	14.86	0.47
Price/Cash Flow (P/CF)	9.49	6.71	8.79	6.67	38.13	4.77
P/E (F1)	20.36	20.46	12.92	3.66	46.66	31.95
Price/Sales (P/S)	1.33	0.25	1.74	0.05	6.02	0.18
Earnings Yield	4.91%	4.91%	7.70%	27.30%	2.13%	3.13%
Debt/Equity	0.77	0.77	0.70	0.88	0.34	0.87
Cash Flow (\$/share)	2.15	1.41	7.01	0.55	0.97	1.41
Growth Score	D	-	-	NA	A	A
Hist. EPS Growth (3-5 yrs)	0.06%	1.51%	10.85%	NA	12.84%	-47.65%
Proj. EPS Growth (F1/F0)	-26.30%	9.42%	5.12%	731.25%	8.68%	145.65%
Curr. Cash Flow Growth	29.33%	2.86%	6.03%	-66.65%	7.29%	-12.07%
Hist. Cash Flow Growth (3-5 yrs)	1.14%	7.19%	8.55%	NA	12.06%	3.49%
Current Ratio	1.13	1.26	1.23	1.26	0.76	2.11
Debt/Capital	43.38%	43.38%	42.57%	46.81%	25.49%	46.51%
Net Margin	6.16%	2.19%	11.57%	0.11%	10.09%	-2.79%
Return on Equity	7.98%	9.37%	16.74%	11.17%	30.34%	-3.19%
Sales/Assets	0.42	1.24	0.54	2.38	1.24	1.15
Proj. Sales Growth (F1/F0)	-4.24%	2.04%	3.22%	5.51%	7.37%	2.04%
Momentum Score	B	-	-	-	B	B
Daily Price Chg	-23.57%	-12.40%	-6.77%	-6.33%	-2.86%	-14.19%
1 Week Price Chg	-18.37%	-18.37%	-11.01%	-0.26%	-4.86%	-28.28%
4 Week Price Chg	-45.69%	-36.32%	-34.65%	-14.75%	-6.80%	-51.13%
12 Week Price Chg	-46.46%	-35.29%	-32.08%	20.72%	12.25%	-57.83%
52 Week Price Chg	-56.84%	-44.36%	-23.52%	-44.36%	-8.71%	-62.62%
20 Day Average Volume	2,490,987	524,648	3,834,688	83,952	1,655,936	251,721
(F1) EPS Est 1 week change	-0.38%	0.00%	-0.06%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-29.27%	0.00%	-0.74%	0.00%	0.42%	0.00%
(F1) EPS Est 12 week change	-29.82%	-0.21%	-1.38%	0.00%	-0.21%	-47.50%
(Q1) EPS Est Mthly Chg	-36.82%	0.00%	-0.85%	NA	0.00%	NA

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	F
Growth Score	D
Momentum Score	B
VGM Score	F

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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