STOCKTRADES PREMIUM COMPANY SUMMARY

PARK LAWN CORPORATION

PLC.TO

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NOTE: DAN IS LONG PLC

Park Lawn Corp provides goods and services associated with the disposition and memorialization of remains in Canada & the United States. It owns and operates cemeteries, crematoriums, and funeral homes. The company generates revenue from the sale of cemetery property interment rights, cemetery services, and funeral/merchandise packages. The bulk of the company's revenue comes from the US.

Our Growth Score: 2.5/5

Dividend Safety Score: 2.8/5

Sector: Consumer Cyclical

Stock Type: Income/Growth

Industry: Personal Services

Our Risk Rating*: Moderate

Current Price: $17.22

1 Year Price Target: $22.99

*Our Risk Rating: Our opinion of the overall risk an investment presents. Can be shown as Defensive (DEF), Moderate (MOD), or Aggressive (AGG). By no means is this an indication of future potential gains or lower volatility.

PROS

- Death is something we cannot avoid
- Consumers sometimes willing to pay more for funerals
- High-margin business
- Not prone to economic cycles
- Valuations have dipped to the point where the stock is quite attractive
- The market is highly fragmented, which leads to plenty of growth via acquisition opportunities

CONS

- Pre-need sales are declining in the tough macro environment
- Not widely covered by analysts
- Dragged down by current growth selloff
- Tendency to issue shares for acquisitions
- Death rates are down 46% on a YoY basis because of a reduction in pandemic deaths, which is impacting the business
- High rates are hitting the bottom line and impacting the overall effectiveness of the company's acquisition based strategy
- The company recently pulled its 5 year guidance

OVERALL THESIS

Park Lawn will continue to make small, bolt-on acquisitions to drive growth for shareholders. Although frustrating, shareholder dilution has proven to be worth it in the long run as prior to its recent correction, the company had put up annualized returns of 14% over the last half-decade, which outpaces the TSX and even keeps up with the S&P 500. The company's aggressive expansion into the US markets and the highly fragmented nature of the business will allow it to fuel growth via acquisition for years to come. Although this is a risky strategy, management has shown it can execute. While this is technically a consumer cyclical stock, this is a company that can provide strong growth in any economic environment.

Yes, pre-need sales are dipping as consumers pinch pennies, which could lead to smaller amounts of capital to fuel acquisitions, but the core of its business should continue to operate without issue. The pandemic and the deaths that came from it were inevitably short-term in nature, and it's unfair to expect the company to continue to grow at the pace it was during that time. However, when we compare the company today to pre-pandemic numbers, it has grown extensively and should continue to do so.

Higher interest rates are impacting earnings, and valuation multiples are being compressed due to the high rates and a lack of interest in small-cap stocks overall. This should allow investors to accumulate at cheaper prices over the short term. The bottom line should reflect this to the upside when interest rates are lowered. In short, patience should pay off with Park Lawn, and our main thesis here is a rebound in earnings once policy rates cool down.

POTENTIAL RISKS

Although the industry is nearly recession-proof, Park Lawn still depends heavily on pre-arranged sales to raise capital for expansion. In a recession, the company may see a fall in pre-arranged sales as customers could pinch pennies and pay on an as-needed basis.

Beta	**1.18**
Alpha	**-15**
Our Risk Rating	**Mod***
Max Drawdown	**60.8%**

Although Park Lawn is the only publicly traded funeral company, it is not the only company in operation here in Canada. There are many companies, and Park Lawn is susceptible to losing market share to emerging competitors. The company's acquisition strategy is working right now. However, growth-by-acquisition is a higher-risk business model, and increased competition can lead to higher valuations, lower synergies, and thus lower returns on capital for shareholders.

The company has some high debt levels. Its enterprise value, which is the market cap combined with debt less current cash on hand, is higher than its market cap. The company has managed debt figures for quite some time. However, investors need to keep an eye on rising interest rates as it is currently cutting into earnings, which is no doubt impacting valuation and investor sentiment.

VALUATION

	TTM	5 Year Average	Industry Average
P/E	**29**	**35**	**49**
P/S	**1.29**	**2.82**	**1.34**
P/B	**0.81**	**1.53**	**3.4**
P/FCF	**13.26**	**21.78**	**20.15**
PEG Ratio(FWD)	**0.33**	**N/A**	**N/A**

Of note, the industry averages listed above are from the personal services industry. Park Lawn has a unique business structure that is difficult to compare to any other personal service. So, take the fact that it is trading significantly below industry averages with a grain of salt.

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Before its recent correction, Park Lawn was valued as a high-growth stock. Although it still has a trailing price-to-earnings ratio of 29, the company is starting to look attractive on a price-to-free cash flow basis.

At only 13.6x trailing free cash flow, the company is trading at a significant discount to its 5-year average. Yes, growth has slowed at Park Lawn due to lower mortality rates post-pandemic and higher policy rates. But, the selloff is overblown. The company's free cash flow per share has grown by over 450% over the last 5 years. So, we consider a 13.6x multiple on that cash flow a bargain.

If we look at valuation from a historical standpoint and if things go as expected for the company, double-digit annualized returns are not out of the question.

Financing costs are materially impacting the company's earnings. This is a company that operates on a lot of floating-rate debt. It utilizes this debt to make acquisitions. When we compare financing costs in 2023 to 2022, they've increased by more than 125%, including the interest on its floating rate credit facilities going up by more than 4x.

The impact to the bottom line via financing costs is causing valuations to dip both via a decline in actual earnings and a multiple contraction due to lower growth because of the higher financing costs. What we mean by this is the market is willing to pay less on a forward P/E multiple for Park Lawn today than it would have a few years ago.

We believe this is a bit short-sighted, and as patient retail investors, we're willing to wait out the storm. A reduction in policy rates should ultimately benefit the company, as the interest at its floating-rate credit facilities currently makes up over 73% of its financing costs. When this happens, we should see earnings improve and multiple expansion on a P/E basis.

COMPETITOR ANALYSIS

	PLC	SCI	N/A
P/E	29	20	
P/S	1.29	2.56	
P/B	0.81	6.41	
P/FCF	13.26	21	

Park Lawn's best comparison is to Service Corporation, which operates the same types of services and trades under the ticker SCI in the US. For a long time, Park Lawn traded at a premium to SCI. However, it has now reversed, and SCI, more than 13x the size of Park Lawn, is the more expensive company. It's puzzling, as SCI's balance sheet and financial position are arguably worse than Park Lawn's. The only thing we can think of is the large-cap stature and more exposure via the US markets are causing SCI to have a lower drawdown than Park Lawn. We still view Park Lawn as the better opportunity moving forward.

DIVIDEND ANALYSIS

Annual Dividend	FCF Payout Ratio	5 Year Dividend Growth %	Dividend Growth Streak
$0.46	34%	0	0

Park Lawn does pay a dividend but a relatively low-yielding one in the high-2% range that isn't growing. So, this section will be short. It aims to provide outsized returns via strategic acquisitions, and as such, there has been no dividend growth. It recently switched from monthly to quarterly payments, which is why one may notice a spike in its dividend paid.

In our opinion, the company would be better suited to stop the dividend and utilize the cash for further acquisitions. However, it is a nice bonus for income investors to not only hold a growth stock, but one that provides a bit of income as well.

RECENT EARNINGS

Earnings Estimates	2024	2025	2026
EPS	$1.11	$1.25	$1.40
Revenue	$419M	$434M	$472M
EBITDA	$100M	$109M	$117.4M
EBITDA Margin	24%	25%	25%

Be reminded that Park Lawn reports its earnings in USD. However, the estimates listed in the table above are CAD, as there are currently no USD estimates for the company.

Park Lawn reported a relatively solid quarter, considering the circumstances. Revenue of $76.3M and earnings per share of $0.215 both topped estimates by low single digits, and the company saw some margin expansion due to the sale of some of its legacy assets.

Revenue declined by 11.9% year over year, earnings by 13.6%, and adjusted EBITDA by 4.4%. However, it is important to understand that these declines were largely expected due to the company's sale of a chunk of assets that it viewed as legacy assets and not aligned with the company's current strategy.

The sale of these assets along with some other operational improvements resulted in a boost to margins. The company's adjusted EBITDA margin jumped from 23.7% to 25.7%.

The company's sale of lower-margin businesses should continue to drive margin expansion moving forward. However, the difficulties for Park Lawn right now remain the fact that floating-rate credit facilities continue to eat away at the bottom line due to higher financing expenses.

The company reiterated its 2024 outlook, in which it expects adjusted EBITDA to be $70M at the low end and $80M at the high end. Adjusted earnings per share are expected to be $0.80 at the low end and $0.90 at the high end. Lower mortality rates, less pre-need spending in light of harsh economic conditions, along with higher financing costs are certainly wearing on the company. However, although lower mortality rates are likely here to stay post-pandemic, two of these issues can be fixed by a decline in interest rates and more spending from the consumer, which is why we're being patient with the company.

Looking at this company objectively, I believe it would be better off eliminating the dividend and allocating capital toward the reduction of debt. Park Lawn currently pays around 30% of free cash flow towards the dividend. With a yield of 3%~ right now and floating rate credit facilities that are much higher than this in terms of interest, the elimination of the dividend and allocating that capital to debt reduction would provide an almost immediate increase in value for shareholders.

When debt gets down to more comfortable levels, the company could reinstate the dividend. Or, they could continue to allocate that capital to more profitable acquisitions, which would likely prove to be more beneficial to investors than the dividend.

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