Q3 2020 Earnings Call

Company Participants

- Debbie Young, Director of Investor Relations
- Eric Tanzberger, Senior Vice President & Chief Financial Officer
- Jay Waring, Chief Operating Officer
- Thomas L Ryan, President, Chairman, Chief Executive Officer

Other Participants

- AJ Rice, Analyst
- John Ransom, Analyst
- Scott Schneeberger, Analyst

Presentation

Operator

Good day, ladies and gentlemen, and thank you all for joining this Service Corporation International Third Quarter 2020 Earnings Conference Call. As a reminder, today's session is being recorded and all lines are in a muted or listen-only mode until the Q&A session at the end of the conference (Operator Instructions).

And with that, I'm pleased to yield the floor to SCI management.

Debbie Young {BIO 16531204 <GO>}

Thank you, and good morning everyone. This is Debbie Young, Director of Investor Relations for SCI. We welcome you today to our company's review of business results for the third quarter of 2020. Before the prepared remarks, let me remind we'll be making some forward-looking statements today. Any comments made by our management team that state our plans, beliefs, expectations, or projections for the future are forward-looking statements. These forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such statements. These risks and uncertainties include, but are not limited to, those factors identified in our earnings release and in our filings with the SEC that are available on our website.

During this call, we will also discuss certain non-GAAP financial measures such as adjusted EPS, adjusted operating cash flow, and free cash flow. A reconciliation of these non-GAAP measures to the appropriate GAAP measures is provided on our website under the Investors Webcast and Events section, also in our earnings press release and 8-K that were issued yesterday. So with that out of the way, let me pass it on to our Chairman and CEO, Tom Ryan.

Thomas L Ryan {BIO 3505123 <GO>}

Thanks, Debbie. Hello, everyone, and thank you for joining us on the call this morning. On behalf of our entire SCI team, I hope that you and your families are staying safe and healthy and finding ways to make the most of these challenging times. This morning I'm going to start by giving a little color our business performance during the quarter. Then I'll provide some commentary on our fourth quarter guidance as well as share some preliminary thoughts on 2021, with the understanding that uncertainty surrounding the effects of COVID-19 pandemic could change that guidance significantly.

Before we get started, let me first say to our entire SCI family, and particularly to our frontline associates, thank you so much for your courage and resolve, and for putting the safety of our client families and teammates first. In our funeral homes, personal care centers, and cemeteries, you care for our client families in our communities during the most difficult of days through the most difficult of circumstances. You provide our families the opportunity to grieve, remember, and celebrate, starting them on the path to healing and closure, which is so important to what we do. So thank you.

Our preneed sales counselors have adapted at a record pace to the use of new technologies and social distancing. You've made it possible for us to deliver peace of mind to our families who wish to develop plans for their future now -- great job, team. If it weren't for the hard work and dedication of our nearly 25,000 associates, none of our success would be possible. When we last spoke in July, we were experiencing elevated deaths from COVID-19, which had resulted in significant growth in our funeral volumes and at-need cemetery revenues for the month of June. Additionally, as gathering restrictions were eased, we experienced unprecedented growth in our preneed cemetery sales production.

While we saw those trends continue into July, we expected the impact to subside during the third quarter. Needless to say we were wrong. These trends continued throughout the entire quarter. Results in both operating segments exceeded our expectations. For the month of October, we continue to see strong year-over-year growth, albeit at slightly lower levels than what we saw during the third quarter. It's a bit awkward and very humbling for us to speak to you today about our financial results for the quarter, at a moment in time that has been so sad, so challenging and filled with so much uncertainty for so many people.

Yesterday, we reported earnings per share of $0.79 for the quarter, compared to $0.37 per share in the prior year. Both funeral and cemetery segments had margin improvement over 700 basis points, driven by double-digit topline percentage growth applied against a leaner cost structure. Below the segments, higher general and administrative costs and a higher tax rate were predominantly offset by a lower share count and lower interest expense.

Let's start with an overview of our funeral operations. Total comparable funeral revenues grew approximately $53 million or nearly 12% during the quarter. Both core and non-funeral home channels performed very well and were slightly offset by lower general agency revenues caused by a decline in insurance funded preneed funeral sales production. Core revenues grew $54 million, driven by an 18.5% increase in the number of cases, partially offset by a 3.6% decline in the funeral sales average.

While we believe most of the increase in cases is due to the direct impact of COVID-19, the CDC has identified approaching 100,000 excess non-COVID-19 deaths, associated with cardiovascular events, diabetes, cancer, suicide, and drug overdoses. We are hearing that the collateral damage effect from restricted mobility, whether government mandated or behaviorally induced, has resulted in deferred or foregone medical care for life-threatening disease screening and limited access to mental healthcare, potentially contributing to these excess non-COVID deaths.

Our discussions with our market leaders support this position. In addition, certain market leaders believe we are gaining market share, particularly in the larger hotspots where our scale can differentiate us from our competition. The 3.6% decline in the funeral sales average was trending positively from the second quarter decline of almost 9%. The cremation mix shift was a moderate 110 basis points. It had a minimal impact on the year-over-year decline. The drag on our sales average continues to be a dip in the funeral and cremation cases with a service attached. Pre-COVID, this percentage was about 63%. In April, it dropped to 40% as the restrictions on large gatherings were implemented. This percentage has steadily increased as restrictions have been lifted and has increased to 58% for the month of September.

Preneed funeral sales production for the third quarter was down just under 3% versus the prior year, an improvement from the 27% decrease versus the prior year we experienced in the second quarter. Two of our top lead sources for funeral sales production, in person pre-planning seminars and in person follow up visits, continued to be down, contributing to the relative decline of preneed funeral sales versus our cemetery sales production efforts. From a profit perspective, funeral gross profit increased $47 million and the gross profit percentage increased 750 basis points to 24%, realizing an 88% incremental margin on our revenue growth. Growth in our high incremental margin core business more than offset a slight decline in our lower margin revenue streams. We also continued to benefit by the efficient management of labor hours, as well as reductions in non-customer-facing costs, and certain marketing and commercial expenses.

Now shifting to cemetery, comparable cemetery revenue increased almost $91 million or nearly 30% in the third quarter. The increase was primarily attributable to core revenue growth of $93 million. At-need cemetery revenue accounted for $24 million of this growth, driven by the higher volume from the effects of COVID-19. Recognized preneed revenues accounted for the other $69 million of core revenue growth, mainly due to higher preneed cemetery sales production during the quarter. Preneed cemetery sales production growth was even more pronounced, growing $95 million or 47% in the third quarter.

Remember, we recognized $69 million in the quarter. Therefore, we've deferred about $26 million of our preneed cemetery sales production growth from the third quarter into the backlog to be recognized as revenues in future quarters. While we're pleased to deliver $20 million of the sales production growth from large sales, the preponderance of the growth, about $60 million of the $95 million, was an increase in core contract velocity of about 35%. This increased sales velocity is being driven by a more productive sales force. Higher at-need activity has generated more highly effective leads, which are more easily converted to a sale.

Additionally, we are seeing a more receptive consumer in general, meaning we're seeing more of an openness or willingness of the consumer in this COVID environment to have the preneed discussion. We also believe COVID has continued -- I shouldn't say -- has conditioned our sales force to more aggressively embrace our customer relationship management system like never before, which has resulted in higher levels of sales counselor efficiency and productivity.

Finally, we also believe customer and counselor incentives designed to differentially drive cemetery production versus funeral, have had a favorable effect on cemetery sales velocity. Cemetery gross profits grew by approximately $55 million, and the gross profit percentage increased 740 basis points to 35%. Growth in revenues and strategic cost reductions were somewhat offset by higher selling costs associated with the significant increase in sales production.

As you saw in our press release, we provided updated guidance for the total year 2020 for adjusted earnings per share, cash flow, and capital expenditures. The ranges are wider than what we typically would give this close to the end of the year due to the uncertainty surrounding the go forward impact from COVID-19.

We base our assumptions on our October results to date, as well as models provided by the Institute for Health Metrics and Evaluation or the IHME that projects future mortality from COVID. Therefore, we would expect to see funeral volume growth and at-need cemetery revenue growth trends in the high single-digit percentage range for the fourth quarter.

Assuming that widespread restrictions on gatherings are not re-imposed, we would anticipate the funeral average to continue to migrate closer to the prior year averages, probably down 1% to 3%. We would expect preneed cemetery sales to continue to grow over the prior year, but at lesser levels than we saw in the third quarter, probably in the high single-digit percentage growth range.

As any company begins to think about 2021, the one thing we know for sure is that we don't know. There never been a less predictable year at least in my business. We've run a variety of scenarios, ranging from a minimal impact from COVID, starting at the beginning of 2021, to a scenario which says November '21 looks a lot like November '20. If these models prove correct, the range for adjusted earnings would be $2.25 to a high as $3.00 per share for the year of 2021. In a scenario where COVID has little to no impact on 2021, we would anticipate funeral volumes to decline in the 12% to 15% range from 2020 levels or a 2% to 5% decline from 2019 levels.

We would anticipate that the funeral sales average would be a very favorable comparison for the year, especially in the second quarter, as we are already experiencing a bounce back towards pre-COVID spending levels. We would expect a preneed cemetery sales production decline in the low to mid-single digit percentages, as we would be comparing to some pretty difficult comps. Even under this scenario, the effect on our earnings per share from improvements we made in our capital structure, the debt refinancing and share buybacks, combined with our leaner operating structure, would produce an adjusted earnings per share result that would meet or exceed our long-term 8% to 12% growth framework on a compounded basis from our 2019 earnings per share base of $1.90.

Our most likely scenario for now is that we might see a continued impact from COVID into the first quarter of 2021, with a lessening effect during the second quarter trending to a more normalized environment by the end of the year. Under this scenario, the quarterly cadence expectation would be significant growth during the first quarter in funeral volumes as well as preneed cemetery sales, followed by a leveling off in the second quarter as favorable comparisons in April transition to a challenging comparison in June, where we experienced excess funeral volume and significant preneed cemetery sales growth in 2020.

The third quarter will be the toughest comparison, followed by a more subdued decline in the fourth quarter. So in summary, I am extremely optimistic about our future. Our team has proved what they're made of during this extraordinary time, and I believe our culture, as strong as it was before, is even stronger today. I believe our actions taken in response to the COVID crisis and our presence both physically and digitally has afforded us selective market share gain.

I believe the accelerated use of new technology required to successfully meet customer needs during COVID has provided many advantages. It will benefit our brand perception and customer loyalty. In addition, the adoption of new technology is producing a more effective and efficient sales model as well as a more nimble service delivery platform. We have improved our fortress balance sheet position with our most recent refinancing, further lowering interest costs as well as extending and improving our debt maturity profile.

Once again I'll close with a sincere thanks to our team. Not only for a terrific quarter, but for the positive difference that you continue to make in so many lives during the most trying of times. Now, I'll turn it over to Eric.

Eric Tanzberger {BIO 1877182 <GO>}

Thanks, Tom. Good morning, everybody. First, and most importantly, we hope that everyone is staying safe in these trying times. Our thoughts remain with the families and communities still faced in the toughest challenges created by this pandemic. And I'd also like to begin my remarks this morning recognizing our almost 25,000 associates who have worked tirelessly to support our communities as we have navigated this pandemic.

The results that we are presenting today directly reflect how our frontline associates have taking on and bravely overcome the obstacles that they affect. To them and to all of our associates supporting those on the front line, we are deeply grateful for the professionalism and poise you have shown during these extremely trying times. So with that, I'd now like to transition to providing some additional color on the financial results. First, I'm going to provide an update on the strength of our financial position that is allowing us to succeed and also be opportunistic in this challenging environment, followed by our cash flow results for the quarter, and I'm going to end my time today with some forward-looking thoughts for the remainder of both 2020 and 2021. So let's start with financial position. And as you know, we are fortunate to have a resilient business model with reliable cash flows that are allowing us to weather the uncertainty created by COVID-19. While we entered the pandemic bolstered by a strong financial position and a favorable debt maturity profile, we continue to be very well positioned with a significant amount of liquidity to first invest in our businesses and then to secondly invest in growth opportunities.

Specifically, our liquidity has remained robust at roughly $740 million, consisting of $220 million of cash on hand, plus $520 million available on our long-term bank credit facility. On a much higher EBITDA generated this quarter, we were able to reduce our leverage from 3.79 times at June 30th to 3.44 times at the end of September as it relates to our trailing 12 month calculation.

Now as we look beyond the impacts of this pandemic into the future, we still intend to manage leverage in the range of 3.5 to 4 times. So let's talk about cash flow and capital deployment during the quarter. In the face of this pandemic, our businesses performed much better in the quarter then our expectations, which were much lower for many of the reasons Tom mentioned earlier.

Ultimately, we were able to generate adjusted operating cash flow results of $195 million during the quarter. When compared to the prior year, adjusted operating cash flow decreased $14 million as cash earnings from the $0.42 of adjusted EPS growth in the quarter was more than offset by $89 million of higher cash tax payments, most of which was timing related, as well as a net use of preneed working capital. So let me walk you through some of these components in a little bit more detail.

The increase in cash tax payment I just mentioned of $89 million was partially earnings driven, but also had some timing aspects as we had deferred $47 million of federal and state income tax payments as allowed by the IRS from the second quarter into this, the third quarter. We also experienced a net use of working capital, primarily related to the substantial growth in cemetery preneed property sales during the quarter, which grew by 56%.

Now recall, the preneed property sales generally have immediate revenue recognition as we're able to deliver this property at the time of sale. However, about 70% of these sales are paid to us on an installment basis primarily over a three to five year period, and that's what creates this working capital use.

So shifting to capital deployment, during the quarter, we deployed a total of $225 million of capital to reinvest in and grow our businesses as well as returning value to our shareholders. Regarding the breakdown, we invested $41 million in the business through maintenance and cemetery development capital spend. While this is lower than the prior year quarter, we have refocused our efforts around these capital projects and expect this spend to ramp up in the fourth quarter.

We have deployed another $32 million into growth through acquisitions and new build opportunities. And finally we returned just over $150 million to shareholders in the form of a dividend and share repurchases during the quarter. So now let's shift to the forward-looking outlook, and let's first talk about 2020. And in the first nine months of 2020, adjusted cash flow from operations has grown $81 million or 17% to almost $560 million.

Now recall that we have benefited from about $30 million in deferred payroll taxes, as allowed under the current Cares Act. So excluding this deferral, we've grown $51 million or 11% over the prior year. When you look to the remainder of 2020, and as you saw in the press release, we are providing updated adjusted operating cash flow guidance of $740 million to $790 million for the full year of 2020. This is in congruence with the higher adjusted earnings per share ranges given and lower cash interest expected as a result of the recent refinancing activities, which are being offset by anticipated higher cash taxes.

So now moving beyond 2020 and beginning to think about 2021, we first acknowledge there are many unknowns, and the pandemic continues to be an ever evolving situation. We have performed extremely well in 2020, and it will be a tough year to repeat. However, we are encouraged by the positive momentum we are currently seeing with preneed sales, expected improvements in the funeral sales averages as COVID eventually gets behind us, and our leaner cost structure.

With all this being said, based on the range of outcomes for adjusted EPS that Tom mentioned, we expect our cash flow in 2021 could similarly range from $550 million to $700 million. There are a few known items impacting 2021 cash flow that are also worth noting. First, we will be required to pay half of the 2020 deferred payroll taxes or $20 million in 2021 and the remainder of that in 2022.

Additionally, we will incur three quarters of regular payroll taxes in 2021, which were able to differ in 2020, which totals about $40 million. These items together collectively create a $60 million headwind to cash flow in '21 when compared to 2020 for payroll taxes. We also expect some cash interest benefits looking into 2021 associated with the third quarter refinancing activities that we just completed.

And lastly, we recognize the importance of reinvesting in our business and expect our maintenance capital spending to return closer to pre-COVID levels as we look to the fourth quarter and into '21. I would also anticipate higher cemetery development spending in 2021 as we complete some high return projects that were purposely deferred earlier from 2020.

So then in closing, I am humbled by the passion and heart of our team members, and I am extremely proud and thankful to all of them who have continued to prioritize the needs of our client families all while performing these services in a very safe manner. It truly is amazing how much we've accomplished this year in such a challenging environment, and I again thank all of our almost 25,000 associates for these tremendous efforts.

So with that operator, that concludes our prepared remarks, I'd now like to go ahead and turn it over for questions.

Questions And Answers

Operator

Certainly. Thank you. (Operator Instructions) We'll hear first from AJ Rice at Credit Suisse.

Q - AJ Rice

Yes, thanks for all the information there. Maybe first off, when you think about the cemetery production you're seeing, obviously it sounds like a fair amount of that is spillover from COVID-related sales, that people are buying multiple plots as they have a death in their family. But can you sort of get back to where you think traditional production is? Is there still a ways to go in seeing that rebound? And I'm assuming you're assuming a more normalized year, next year when you -- as you get back to next year. Is that what is part of the strength in the guidance is all about?

A - Thomas L Ryan {BIO 3505123 <GO>}

Hey, I think that's correct. We mentioned -- I think I mentioned four different things that we believe are kind of impacting sales. And while you're right, the at-need activity is a part of it. I would say it's clearly not near a majority of it. A lot of what we believe we're seeing is this openness of the consumer to have the discussion around preneed and the importance around it, and there are some other things that are driving it. Like I said, I believe we're managing the process a lot better with our customer relationship management system, because again we were precluded from traveling, right. So we're sitting there with Salesforce driving activity through the management process, and that's been more effective. So I think as we think about the coming years, clearly at some point, hopefully soon, this at-need traffic is going to slow down, and that's going to have a year-over-year issue for probably particularly June of the third quarter. But I also believe that this focus of the consumer may last beyond it.

I don't think this is something that everyone is going to forget right away. And I think the intention of the consumer could continue. So we're pretty excited about the opportunity to have a conversation to provide that peace of mind to our families so they take care of that and something that's truly important. I think what's going on now just reinforces to everybody how important this is. So we feel good about it. Obviously 2020 is going to be a tough comp. But we feel good about 2021 and beyond.

Q - AJ Rice

Right. So in the sales per case decline in the third quarter was down 3.6, sounds like you think it will improve a bit in the fourth quarter. Is it still primarily a bifurcation that your Canada operations and maybe California are a little worse than that given the locked down situation and the rest of the country's closer to even? Then what do you think -- how are you thinking about that angle when it's in next year? Are you thinking that you'll see some further easing in the restrictions in Canada and California or are you more optimistic about the rest of the country just picking up more?

A - Thomas L Ryan {BIO 3505123 <GO>}

We saw actually both Canada and California improve, particularly in the back half of the third quarter. So we didn't see that big differential change. It's still slightly different, but not that big. So really across the whole network, we're seeing a normalization. Now clearly people are not having as large a gathering. And as we shared with you, our attachment rate for service used to be 63%, it dropped to 40%. It's now back to 58%. If you bifurcate that, the burial consumer is pretty close to par, kind of back to the same level.

And we're seeing a little bit of a stubbornness of, even though we've seen improvement on the cremation side, where a lower percentage of people are choosing service with cremation, and we too think that will improve. So we feel better. The other things that are impacting it are clearly people are not buying as much catering, a lot of the ancillary things that they traditionally would buy. So as we begin to open up more, we expect those categories to be selected and see a return to revenue growth.

Q - AJ Rice

Okay. And then one last question, you mentioned in the prepared remarks, Tom, that you think you maybe picking up vis a vis local competitors. Just wondering what do you think is driving that? Is you're better able to handle the COVID situation, is that what's driving that? Or what do you think is driving that? Do you have any sense of how much of a share shift we might be talking about?

A - Thomas L Ryan {BIO 3505123 <GO>}

Sure. I'll follow up. But I'd like to -- Jay Waring, our Chief Operating Officer is here, and he's had a lot more discussions I think with some of our markets. And Jay, you want to share a little insight, and then I'll follow up the last part of his question.

A - Jay Waring

Yeah, one thing we're seeing about this problem is a tremendous focus on safety, a tremendous focus on quality, with PPE, with cleanliness. We actually added a question to our JD Power survey of April to the families that use us that ask, did you feel safe and cleanliness of the location when you visited our location? And over 99.5% of families said yes.

So anecdotally, we were in Los Angeles a couple of weeks ago. And the team at Rose Hills said, "we believe we are gaining share because we have a reputation in our community of safety and cleanliness. They feel comfortable coming here for gathering and for services as do the clergy."

A - Thomas L Ryan {BIO 3505123 <GO>}

And AJ, from a digital perspective, we rolled out our every detail remembered campaign, and we are having much higher digital presence.

There is a lot more people flowing through the websites, there's a lot more people on social media. So I think again, with the scale that we have, with the expertise in that area that we have in the company, we are getting our message out more and more, more effectively. So I think from a physical interaction with the consumer and with a digital interaction with the consumer, our awareness is up, and we feel like we're seeing numbers that are above our expectations, again both in the, let's say, the hotspot markets and throughout the network.

Q - AJ Rice

Okay, thanks a lot.

A - Thomas L Ryan {BIO 3505123 <GO>}

Thanks, AJ.

Operator

Our next question will come from John Ransom at Raymond James.

Q - John Ransom {BIO 1535724 <GO>}

Hey, good morning.

This may be a hard question, but how should we think about -- let's just imagine a world where volumes next year and volumes this year are sort of in sync. So we're stripping out the variable costs. How should we think about the permanent cost structure on kind of a like-for-like basis and what costs you've been able to take out during this year?

A - Thomas L Ryan {BIO 3505123 <GO>}

Sure, John, and I would only expect that type of question from you, a good one. So there's a lot of learnings, John, on the cost side. And the first one I'll touch upon, because you go through the crisis -- you know, this is a question, you've asked this for 15 years, 20.

Do you have flexibility in your network in order to handle? And I think what we found out, and I always told you yes. And I guess I didn't really know the answer, and now I do. The truth is, we did a tremendous job. Our teams are so talented, and the tools that we have to do it. I'd say through the learning process what we found is that we probably weren't utilizing the clustering concept to the maximum benefit, because we got in positions where we said we really don't have enough part time labor or they are not available. As I said, we probably did a much better job of sharing resources than the company's ever done, partially, out of necessity but partially out of nimble local management and just being smart about it.

So I think we learned better how to utilize our labor force through this process more effectively. The other thing is we have a lot of -- and this is a corporate American issue, a lot of travel and entertainment goes into almost 25,000 employees. I think what we learned is when we didn't have it, we did pretty good. It doesn't mean we won't have it going forward, but I'd say the levels as we think about those types of things from travel and entertainment to seminars to ways that we leverage marketing or leads. We learned a lot in that piece. And I think -- and again, I touched upon it earlier, you'll probably see we've really driven down the cost per lead, and we're utilizing digital leads much more effectively, which are a lot cheaper than our traditional lead methods.

So I think we just found better ways to operate as we move forward. And on the backs of that, John, I think what's interesting -- because these are all things that we did with existing technology. We're now in the midst of we call it a Reimagine project which is taking -- leveraging technology to the next level, into really every facet of service delivery.

So we've accelerated a lot of that through this crisis to try to get there even quicker, and that's going to allow us, I think again to become even more efficient, more effective, and most importantly, I think more nimble in delivering service to our client families.

So a lot of good news around that, and I think there are near-term benefits that will benefit '21 and '22. I think longer term, Reimagine will allow us to further leverage our cost structure.

Q - John Ransom {BIO 1535724 <GO>}

So, Tom. That was, as usual, a beautifully eloquent answer, but it didn't have a single number in that answer. So maybe -- is there a number that you could attach to any of this? This is math question. I bet you did well on essay questions in high school, but this is a math question.

A - Thomas L Ryan {BIO 3505123 <GO>}

I did. I just put B on all the answers on the math section. It's hard to pin down an exact number, but I guess the way, I would say is this way, I believe that even even today if you look out into 2021. First is the cost structure, let's call it a 2019 cost structure because '20 is going to be a weird one. We've probably identified somewhere in within a range of $10 million to $20 million of savings, as you think about the way that we're doing it today.

And I believe we're just getting into that, like I said, I think when we have the tools with Reimagine, we'll be in a position to drive more efficiencies as we begin to think about how we service clients and what we do. So I'd say that's probably a fair number to think about it today, somewhere in that neighborhood.

Q - John Ransom {BIO 1535724 <GO>}

All right. That's it for me. Thanks so much.

Operator

Once again, (Operator Instructions). We'll hear next from Scott Schneeberger at Oppenheimer.

Q - Scott Schneeberger {BIO 5302695 <GO>}

Thanks very much. Good morning, all. If we could start with the guidance for the balance of this year. I believe I heard it was high single-digit cemetery preneed growth in fourth quarter. That follows 46% in third quarter. I'm just curious, it seems conservative based on trends we hear in the market and that you're commenting on in October.

So in -- just curious on how that that is being looked at. And also if you could please work into the answer consideration of the recognition trend in preneed? Thank you.

A - Thomas L Ryan {BIO 3505123 <GO>}

Sure, Scott. So, you think about cemetery, two things to consider. We're comparing against probably an easier comp when you think about third quarter of last year, so when you look at the percentage change. And we had a pretty strong fourth quarter. So to start with, I'd say the comps are different. And then the second thing I believe part of this is -- remember we had the second quarter -- I don't want to use the word standstill, but when you look at the month of April in particular, activities were down dramatically.

So there's probably a little bit of a catch-up factor that rolls into this 47%. That's probably not a number I'd get used to. I'd love to get used to it, but I don't believe it. But what we are seeing and continue to see is this consumer that is ready to have a conversation. So you maybe right, maybe high-single digit ends up being a little conservative. But I think it's more in the ballpark of what we'd anticipate and kind of what we're seeing as we're out of the gate in October.

So I think that's probably the better way to think about it, and that would be -- my two biggest reasons are catch-up from the second quarter and the comparable issue. As far as recognition goes, we traditionally -- the fourth quarter is typically more of a recognition spillover just because of the -- Tammy will kill me -- the word cadence, the cadence of the projects, it tends to fall in the fourth quarter. So you will see a catch-up I would expect in recognizing some of the revenue that we sold in the backlog today.

So that will be a change. That will be a change when you think about 2021 of next year. We're anticipating probably spending somewhere in the neighborhood of $100 million on cemetery inventory development. And so we think about 2021, I would expect that number could be even higher when you think about a recognition percentage.

Q - Scott Schneeberger {BIO 5302695 <GO>}

Okay, thanks. Appreciate that. Yeah. And that was going to be my next question. You somewhat answered it, just how the recognition flows and spills into -- it's certainly the first part of 2021 throughout. I'll move on from that though. Eric, you covered some discussion on use of capital, just curious what the company stance is with regard to M&A. In this environment, you talk about differentiating versus peers. We've heard it out in the industry, the technology factor of Service Corp certainly is a differentiator in this environment. So it just curious on M&A and and also thoughts with regard to using capital on stock repurchase? Thank you.

A - Eric Tanzberger {BIO 1877182 <GO>}

I'll take the first part of it, M&A. Scott, you've known us long enough where we've been very consistent, and we're not really deviating from our plan. And that is, you look at the highest relative return opportunity, and M&A is going to win in those situations. I do agree with you that I think we are starting to bring things to the table in terms of really hitting on all cylinders in the category as we've described to investors before in our Investor Days, just leveraging our scale and utilizing of technology.

And I think I also would kind of echo Tom's comments. I really think we're kind of in the early innings of that to be honest with you. I think some of the stuff that we're doing now and are going to put capital behind, such as the Reimagine project, I think are going to be even more of a differentiator. That's not moving the M&A needle today because it hasn't been executed upon, but I think people are starting to notice. And I think it will move the needle, frankly, in the future as more of a differentiator to us.

So when you think of M&A being a kind of the highest relative return from a kind of a after-tax IRR perspective, then you look at what's next, and it's probably new builds. So both the first things that we're doing -- of course, none of this is done without reinvesting in the business. So the first thing we're doing is maintenance CapEx and cemetery development. Then with that excess cash flow, after we're comfortable that we reinvested appropriately into the business, we're looking at M&A and new builds.

Newbuilds has a slightly less return M&A because it takes a couple of years to get to EBITDA stream up and running, but it's very successful into the low-double digits percentages. The dividend, we know about, as we've said, we're going to continue to -- we feel very strongly about having a dividend. And we'll continue to grow the dividend commensurate with how the company is growing. And I think the last resort is probably in the shares. And I think one thing that I'll comment on, as you see our track record in shares, is that we have taken very seriously the differential return of those shares versus what we believe the true intrinsic value is of those shares.

So you have seen us at certain points shutdown shares, and you've seen us at certain points be very aggressive. So not only is that relative to M&A and new builds, and it frankly doesn't really beat those returns, but it's very relative amount among kind of a spectrum of what we're used to seeing in terms of that return with shares. At the levels that you saw during the pandemic, and specifically during the third quarter, we think it's a very good use and a high return opportunity relative to past returns for share repurchase program.

And that's why you've seen us execute on it as we have. But I want to be very clear. The first thing we're doing before we do that is reinvesting in the business and going to the higher relative return opportunities, such as M&A and new builds.

Q - Scott Schneeberger {BIO 5302695 <GO>}

Thanks. So it's just a quick follow up on that and then one more. On M&A, are there ripe targets or is this an industry that's just incredibly distracted right now, and that's not something that can actually happen right now or is it?

A - Eric Tanzberger {BIO 1877182 <GO>}

No, it's happening. And I think there has been some disruptions. As you know, it's out there. Jay kind of alluded to it in terms of us being able to withstand this and leverage our scale. And other people probably struggle a little bit to maybe do that, that don't have the scale and the wherewithal to get through some of it. So with that came what we think is maybe a little bit of market share, especially in the hotspot markets. And I'd also say that that's kind of brought a little bit more life to the pipeline, we obviously don't -- we report quarterly.

So we reported our Q3 numbers there, but I would just characterize it as it's coming life. And I think we're kind of excited about what we're seeing in terms of the pipeline.

A - Thomas L Ryan {BIO 3505123 <GO>}

Scott, I just add to that. There's a candidate that's got a 39.6% right on capital gains out there. If it went that direction, I do think that's going to motivate a lot of people. So we are poised and ready to talk if that were to occur.

Q - Scott Schneeberger {BIO 5302695 <GO>}

Interesting dynamic, Tom, thanks. And then lastly, just looking for an update on the funeral rule, I'm guessing that's been probably a back burner topic. But I know you check in with the FTC on occasion. Just curious what the status is there?

A - Eric Tanzberger {BIO 1877182 <GO>}

Yeah, status is somewhat frankly quiet since the last time we talked. We concluded -- everybody, the industry and everyone who wanted to publicly comment, concluded those comments with the FTC -- kind of mid-June was their cut off. And so I really don't have an update since the last conference call which was late July.

The process is, Scott, as you know that the commissioners and the staff primarily will look at this and digest all these comments. And then they'll go and decide internally whether they want to -- what they want to do. And if they choose to move forward with something, it kind of resets the process. Whereas there's a little bit of an indication of what they want to move forward with or consider, and then we have an adequate time period to not only submit in writing, but there will potentially, if past is true of the future, there will potentially be some, probably some hearings and in-person meetings as well associated with that -- with that process. With the election right here and everything going on obviously in the world, I'd be very, very surprised if there is something imminent. If there is, I'm not aware of it. I just think that may delay a process that's already got a lot of meat to it because there's a lot of comments that they're going to have to kind of go through and file and digest along the way.

Q - Scott Schneeberger {BIO 5302695 <GO>}

Great, thanks. Appreciate it guys.

Operator

And ladies and gentlemen, that does conclude our question and answer session. I will turn it back to SCI management for any additional or closing remarks.

A - Thomas L Ryan {BIO 3505123 <GO>}

I want to thank everybody to read on the call today. Please stay safe, take care of yourself, and again make something good out of this strange time. We'll talk to you again, our fourth quarter earnings call which will be early February. Thank you so much.

Operator

This does conclude today's session. We thank you all for your participation. You may now disconnect your lines, and we hope that you enjoy the rest of your day.