# Q2 2022 Earnings Call

## Company Participants

- Debbie Young, Director, Investor Relations
- Eric Tanzberger, Senior Vice President and Chief Financial Officer
- Tom Ryan, Board Chairman, Chief Executive Officer and President

## Other Participants

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

## Presentation

### Operator

Good morning and welcome to the SCI-shared second quarter 2022 earnings conference call. All participants will be in listen-only mode. (Operator Instructions) Please note this event is being recorded. I would now like to turn the conference over to SCI management. Please go ahead.

### Debbie Young {BIO 16531204 <GO>}

Thank you and good morning. This is Debbie Young, Director of Investor Relations. Today, we're going to be providing an overview of our business results for the second quarter. As usual, I'll quickly go over our Safe Harbor language before the prepared remarks. 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.

In today's call, we'll also discuss certain non-GAAP financial measures. A reconciliation of these measures to the appropriate GAAP measures can be found in the tables at the end of our earnings release and also on our website under the Investors section, Events and Webcast. To begin our prepared remarks, I will hand it over to Chairman and CEO, Tom Ryan.

### Tom Ryan {BIO 3505123 <GO>}

Thanks, Debbie. Hello, everyone, and thank you for joining us on the call today. First of all, I want to express my heartfelt thanks to our entire SCI team. It is your perseverance and commitment that positioned us for the results we posted this quarter. More importantly, you've continued to stay relentlessly focused on what we do best, helping our client families and our communities gain closure and healing through the process of grieving, remembrance, and celebration.

Now to the business at hand. This morning, I'm going to begin my remarks with a high-level overview of the quarter, followed by some further color on our business performance for the quarter, including some detail around our solid funeral and cemetery results. For the second quarter, we generated adjusted earnings per share of $0.84, an $0.08 decrease over the prior year quarter of $0.92, which experienced a more significant pandemic impact. For a better perspective of this quarter's performance, we delivered earnings per share growth 45% above 2020 and 79% above a pre-pandemic 2019 second quarter. Compared to the 2021 second quarter, the funeral results were relatively flat but well ahead of our expectations, as we continued to see elevated levels of funeral services with a strong funeral average.

On the cemetery side, profitability was below prior year, as preneed cemetery sales production, while still historically very strong, was down about 3% versus the 2021 second quarter. Additionally, Cemetery Trust Fund income declined, as it was impacted by steep declines in the equity and debt markets during the second quarter. Over the quarter, we saw a $0.03 decline in earnings per share from operations, both comparable ops and acquisitions, and a $0.05 decline below the line, as higher general and administrative costs primarily impacted by the timing of incentive accruals and a higher tax rate were somewhat offset by the favorable impact of a lower share count.

Now let's take a deeper look into the funeral results for the quarter. Total comparable funeral revenues grew nearly $10 million or about 2% over the prior-year quarter, exceeding our expectations, as growth in core revenues and recognized preneed revenue were slightly offset by a reduction in general agency revenue. Comparable core funeral revenues grew over $3 million led by an impressive 3% increase in the comparable funeral sales average. Our percentage of families selecting to have funerals and celebration of life services has essentially returned to pre-COVID levels. In conjunction with the rollout of our Celebration of Life Initiative, we are seeing families selecting upgraded facilities at a higher propensity, to select catering and flowers. This increase in average was achieved despite a 170 basis point increase in the core cremation rate. Comparable core funeral volume declined about 2% compared to the prior-year quarter, slightly offsetting the positive impact of the funeral sales average.

Keep in mind that 2022 second quarter volume is still over 6% higher than the pre-COVID 2019 second quarter. And we're continuing to serve elevated levels of client families above and beyond COVID deaths, which is consistent with our commentary around this topic during our Investor Day presentation in May. Recognized preneed revenue increased over $9 million or 28%, as increased digital leads and a more effective direct mail strategy successfully drove more contract velocity within our talented SCI Direct team. From a profit perspective, funeral gross profit increased almost $4 million, while the gross profit percentage increased 30 basis points to 21.6%. Revenue growth of $10 million resulted in about $4 million of incremental profit. Lower margin growth from flowers and catering as well as higher merchandise costs slightly reduced our expected profitability. Preneed funeral sales production grew over $7 million or nearly 3% over the second quarter of 2021. Our SCI Direct production was particularly strong, posting an increase of almost 20% over the prior-year quarter. The increased contract velocity driven by a new and more effective targeting strategy for our direct mail and seminar programs, as well as increased digital leads, were the primary drivers of our growth.

Now shifting to cemetery, comparable cemetery revenue decreased $18 million or about 4% in the second quarter. In terms of the breakdown, core revenue was down by $12 million compared to the prior year. Atneed revenues were flat, so recognized preneed cemetery revenues accounted for the decline. Other revenue decreased by about $6 million over the prior-year quarter, as Endowment Care Trust Fund income was negatively impacted by prior-year capital gain distributions that did not reoccur. Preneed cemetery sales production declined by $11 million or about 3% in the second quarter. We must keep in mind, we're comparing against a 2021 second quarter that grew by 36%. Said another way, our second quarter 2022 sales production is 45% above our pre-COVID second quarter 2019 sales production.

As we referenced in our Investor Day presentation, we believe we have enhanced our sales and marketing productivity in cemetery sales from learnings achieved during the pandemic. We're experiencing a slight decline in sales velocity that is for the most part being offset by increases in the core sales average. Large sales have remained robust but down slightly by $2 million as compared to the prior year. We have seen a slight decline in appointments held, as this discretionary consumer diverted their attention to increased travel and societal engagements this year after post-COVID related lockdowns, and also felt the impact of general inflationary consumer pressures. The good news is our close rates continue to improve year-over-year, and with the strength of both our sales team and our customer relationship management system, these opportunities are not lost, rather deferred and should bode well for future sales production.

Cemetery gross profits in the quarter declined by about $14 million and the gross profit percentage dropped 170 basis points to 33.7%. Declines in high margin merchandise service and Internal Care Trust Fund income accounted for most of the gross profit decline. As you saw in our earnings release, we reaffirmed our 2022 adjusted earnings per share range of $3.30 to $3.70, or a midpoint of $3.50. We remain very confident in the range that we provided you. In the (technical difficulty) segment, we're continuing to see volumes above our expectations with a continued strong average revenue per case. Preneed funeral sales are trending slightly below our expectations as the discretionary consumer seems to be slowing down a bit. We're experiencing some inflationary pressure that we had anticipated and are, for the most part, recovering with inflationary pricing. On the cemetery segment, our atneed revenue is trending higher than expectations due to stronger volumes, while our preneed sales production is slightly behind our expectations due to a slight decline in velocity that we believe is attributable to diverted consumer attention and general inflationary pressures.

The good news is that we have quite a bit of completed construction projects scheduled to occur particularly in the fourth quarter that have a very healthy backlog of sales and will be recognized as revenue upon completion. We are also, are experiencing some elevated labor maintenance costs in our cemeteries, both internally and with third-party vendors. However, these are not material to the company as a whole and for the most part, are being recovered with inflationary pricing. Below the line, we saw and continue to expect variable interest rates to move up. The tax rate expense incurred in the second quarter had a $0.03 incremental negative impact on earnings per share. This was associated with the sharp decline in the financial markets, so we do not anticipate this reoccurring in the back half of the year.

With that, Operator, I'll now turn the call over to Eric Tanzberger.

## Eric Tanzberger {BIO 1877182 <GO>}

Thanks, Tom. Good morning, everybody. Now I really want to start with the most important thing and that's really thanking our 24,000-plus associates that have helped us produce these impressive financial results this quarter. Everybody in the field, you continue to provide exceptional service to our customer families and all of our communities during these exceptional circumstances, while also managing through the COVID era and taking us beyond that era. So hear me very loud and clear, thank you for everything that you do for our company.

So with that being said, I'd like to discuss, on the rest of the call, our cash flow results, capital investments for the quarter, some of the market effects on our trust funds, and then provide some comments on our cash flow outlook for the remainder of this year. So we generated operating cash flow of $141 million in the second quarter. This is in line with our expectations. It was about $50 million lower than the second quarter last year, that again was impacted by COVID-driven positive activity. Similar to our adjusted earnings per share, these current cash flow results are significantly higher than pre-COVID activity levels, such as the $84 million of adjusted cash flow we generated in the second quarter of 2019.

So for this quarter though, versus second quarter last year, our cash flow was reflective of the $18 million decline in operating income which excludes gains on divestitures, $15 million of higher interest and cash taxes, as well as about $17 million or so of an increased use of working capital. The cash interest payments were on target, increased an expected $10 million, predominantly associated with debt restructuring transactions which we did in the second quarter of last year, as well as a smaller impact from increases in our floating rate debt. Additionally, the cash taxes slightly increased in the quarter over the prior year, which was in line with our expectation. And this increase was only about $5 million for a total of about $95 million. The net use of working capital in the quarter was really related to timing of some payable outflows, really between the first quarter of this year and the second quarter of this year. So think of that as really just timing.

Now let's shift gears and talk about the impacts of the trust funds. Obviously, if you've seen, the volatility of financial markets has impacted the market value of our trust funds that support future revenues tied to contracts in our preneed backlog. I'd like to most importantly remind everybody that this has a muted effect on our near-term earnings and our near-term cash flows. So given the 10-year to 14-year average life of the customer contracts, only about 8% of those contracts in the trust backlog mature in any given year. Therefore, the effect on the reduction in trust fund market value allocated to each individual contract is really reflected in our earnings and cash flows over a 12-year period or about 8% per year. Hence, the muted effect that I'm referencing.

More specifically at June 30, our trust funds had decreased about 15% year-to-date and ended this quarter with a $23 million net unrealized loss in the totality of the funds. However, the trust funds have recovered significantly this month since June 30 after the quarter, and we are currently in a net unrealized gain position of just over $200 million. We are currently modeling our trust to end the year down in the mid-single-digit percentage range. Now I want to touch upon our capital investment activity. During the quarter, we invested $245 million into our existing businesses, new build opportunities and accretive acquisitions, as well as returning capital to our shareholders. Let's talk about the breakdown.

We invested about $84 million into our businesses, consisting of $53 million of maintenance capital, which by the way, was higher than both our expectations and the prior year, as we really accelerated the completion of several field technology and other field infrastructure projects into this quarter. Additionally, we invested just over $30 million into cemetery development projects during the quarter. This was higher than the prior year, primarily due to the COVID-related delays that were experienced last year. We view these higher investment levels in both maintenance and cemetery development as timing related, and we are reiterating today our $270 million to $290 million maintenance and cemetery development annual investment guidance for the full year of 2022.

From a growth capital perspective, we deployed $50 million towards the purchase of real estate, construction of new facilities and expansion of existing funeral homes and cemeteries across our footprint. On the acquisition front, we had a small transaction closed in the Mid-Atlantic region for only about $2 million. However, after June 30, we closed on another transaction on the West Coast. Currently though, we have several pending transactions in various stages and we anticipate having what we would call a robust second half of acquisition activity this year. We remain very pleased with the acquisition pipeline and we believe we will end the year at the higher end of our range of $75 million to $125 million of investment and accretive acquisitions. Finally, we continued returning capital to shareholders, with nearly a $144 million being returned this quarter alone through dividends and share repurchases.

Now I'd like to shift to a few comments about our financial position. We continue to have a strong balance sheet with a favorable debt maturity profile and great liquidity of just over $930 million at the end of the quarter that consisted of about just over $200 million of cash on hand, plus almost $730 million available on our long-term bank credit facility. Additionally, our leverage at the end of the quarter was just under 2.7 times net debt to EBITDA. We will continue in the second half to invest capital in high return opportunities such as the acquisitions I just mentioned, new builds, and our share repurchase program. We will also comp higher EBITDA quarters from the prior year that were positively impacted by COVID activity. The result is our expectation for our leverage ratio to increase from this level today and to end 2022 in the lower end of our targeted leverage range of 3.5 to 4 times.

Now let's talk about the outlook for the remainder of 2022. We remain very comfortable and we reiterate our annual guidance for adjusted operating cash flow of $750 million to $800 million again for the full year of 2022. We have already generated $473 million of adjusted cash flow towards this annual target in the first half alone, partially boosted by the COVID activity in the first quarter. Our annual guidance incorporates an anticipated decrease in COVID-related activities for the remainder of this year, resulting in lower cash flows when compared to both the -- this first half momentum I just mentioned, as well as the second half of the prior year. Included in this confirmed guidance is a slight adjustment to our previous cash tax payment estimate of $180 million to now be in a range of $180 million to $190 million.

And while we're on the topic of taxes, from an effective tax rate standpoint, we now expect a range of 25% to 26% for the full year compared to previous guidance of 24% to 25%. Our rate expectations changed primarily due to non-deductible losses incurred from the negative financial returns on cash surrender value of certain life insurance policies we hold. This caused our effective tax rate percentage to increase in the quarter. Finally, I would also like to make some comments on our corporate G&A during the first half of the year. This corporate G&A has been trending higher than our normal quarterly run rate as a result of higher annual ICP [ph] accruals linked to current operating results, as well as our long-term compensation plans that are tied to increases in our total shareholder return that have been pretty healthy.

As we look to the back half of this year, we do expect to revert to our normal quarterly G&A trajectory of $37 million to $38 million per quarter that I talked about and discussed with you on the February call earlier this year. So in closing, through the first half of this year, we are very pleased with our financial results and are excited about our continued momentum as we look to the back half of this year. Most importantly, I would also again like to thank all of our 24,000-plus SCI associates for helping to achieve these great results and serving the client families that you do so well.

So with that, Operator, I would now like -- that ends our prepared remarks from Tom and I, we'll go ahead and pass it back to you and open the call up for questions.

# Questions And Answers

## Operator

We will now begin the question-and-answer session. (Operator Instructions) Our first question is from Joanna Gajuk of Bank of America. Please go ahead.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

Hi. Good morning. Thanks so much for taking the questions here. So I guess you mentioned the cemetery preneed sales rate declining year-over-year, but still running pretty healthy versus the pre-pandemic levels. So I guess two questions here, the first, I guess when you talk about the 45% above the pre-Coronavirus pandemic levels, is there a way to think about the breakdown for this number, how much is due to higher velocity and how much is from higher average price?

## A - Tom Ryan {BIO 3505123 <GO>}

Yes, Joanna, I don't have the (inaudible) compared broken down, but I think just from speaking from using approximations, we are -- I think all three trends look very favorable. Our velocity is higher quite a bit, probably in the high single digits. We've seen some -- some healthy increases in sales average as we've invested in cemetery property and upgraded the cemeteries, and our large sales activity, again, is more than double-digit percentages higher. So really firing on all cylinders.

And I think the one thing I was just pointing out is, we knew that last year was probably the peak, right? You had a lot of COVID activity, you had a consumer that was, for all intents and purposes, kind of locked down and not anywhere to go. And two, you really haven't seen any signs of inflation incurring in the economies of the perfect world. And the only difference we're beginning to see, and some of this is our speculation, is we're seeing some of the consumers, particularly at the middle on the bottom of the socioeconomic demographics, seeing them pull back a little bit. And again we're speculating that's gas prices, that's electricity. Is it a good time for me to start a three-year payment on the cemetery property? Probably not. I'd like see things settle out. The good news is, and that's what we're trying to point out, these are -- these are leads that we have maintained relationships with. And so, as things settle out, we expect we'll go back and close those contracts.

But that's really it and I think too you've got a consumer that -- I mean, you're seeing the airports and the lost luggage in Europe, I mean people are out doing stuff, not just traveling, but they're going to shows and doing different things. We've also seen some unique things like COVID resurface. I know one region of our Company and the sales region, we had, I want to say 40% of our sales counselors out either on vacation or with COVID, you got customers with COVID. So I think we just had a little bit of a difficulty that we expect to begin to work out of. We still have a very high propensity for customers to want once we get in front of them. Our close rates are the highest they've ever been in the Company. So we feel really strong. We just wanted to point out, we are seeing a little bit of a consumer inattentive as compared to a very attentive last year second quarter.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

And I guess too there, that actually that -- that was my other question also. In terms of this dynamic, in terms of the preneed cemetery sales, maybe some impact there. And I guess in the quarter, it was down year-over-year, obviously very tough comps to start out, but last time you were talking about expectations for the preneed cemetery sales to increase low single digits for the year despite a tough comp. So is it still the expectation for the full year?

## A - Tom Ryan {BIO 3505123 <GO>}

Yes, I think we can -- we believe we're going to get back to slightly positive for the year when you look at the cumulative effect or right around there. I mean, surely, still feel pretty good about getting back to levels for the whole year, because we had a really solid first quarter as you'll remember, I think we're up over 10%. We're going to eat away at that. I think if you think of the back half of the year, we'll probably be slightly down, but a cumulative year that achieves the same level as 2021 or thereabouts.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

And I guess this also is linked to the recognized cemetery revenue. So you mentioned last quarter, of -- this 15 large projects that have been developed across the country and that you expect to record a $35 million revenue over the rest of the year and maybe into early next year. So are these on schedule, timing for when you might expect these revenues to come through? Is this kind of -- tracking as you were -- were expecting things when we last time talked about it?

## A - Tom Ryan {BIO 3505123 <GO>}

We are, Joanna. I think particularly in the fourth quarter, we anticipate having a lot of completed construction projects. And like I was kind of referencing in my comments, we've really been selling hard into those. So I think the impact on -- your -- to your point, recognized preneed revenue is going to be pretty significant when you think about the fourth quarter. So probably going to recognize more than we sell in the fourth quarter by quite a bit. Probably not the same dynamic in the third. But again, we will have some completed contracts in the third quarter too.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

Okay. So -- and I guess, there are no delays in terms of just you mentioned some other things, but it sounds like these are on track?

## A - Tom Ryan {BIO 3505123 <GO>}

That you're right, I think we feel good about the timing on all this.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

Okay, and if I may just add a very last question. So you mentioned -- because I was also thinking in terms of delays and things around just the labor, because you know -- or I guess the -- I cover the healthcare services providers, so they talk about a lot of shortages and I guess you also mentioned like salespeople out on vacation or actually down with the virus and whatnot. So can you just talk about what you see on your labor front in terms of your -- either just people not available for -- does that create any issues? And then I guess also on wage increases, what do you think there given the inflationary environment we are in? Thank you.

## A - Tom Ryan {BIO 3505123 <GO>}

So if I bifurcated by funeral, on the funeral front, we're probably seeing overall wage increases in the 4% to 4.5% type of levels. Now, what that's composed of is two different things. One is, because we have more, I'll call it robust funeral services this quarter versus last year's second quarter. Remember, you still had a little bit of the lockdown effect and not as celebratory on general level. So we'll probably have more hours of labor when you think about overtime and things like that, servicing a similar level of cases. But we're also seeing a little wage inflation, particularly in certain markets. And our philosophy, like I said before, led by Jay Waring, our Chief Operating Officer, is as we experience those, our local teams are sitting down and saying we've got issues, let's give these wage increases, now let's find a way to put this on the price list.

And again, we do a fantastic job and we want to be able to -- to charge appropriate rates for our great people. So we're managing that away I'd say, we're not seeing the same level as you're probably hearing about, but it is a little higher than normal. I mean, inflation is creeping into that. On the cemetery side, it's probably a little bit more. Some of our cemetery maintenance is internal and some is third-party contracts. On both fronts, we're definitely seeing some inflationary increases that we've absorbed. And they are probably in the higher range, kind of a higher-single digit. We've had those in place now for a couple of quarters, so it is not brand new. And again, we're trying to manage as best we can, and again, pass along those costs to the consumer as we go through our annualized pricing. So we feel good about being able to cover those through pricing, but we're seeing a little bit of that creep in and as you would anticipate, but again, nothing -- like I mentioned in my comments, it's not a material event for what we do.

## Q - Joanna Gajuk {BIO 16689444 <GO>}

Thanks, Tom. Thank you.

## A - Tom Ryan {BIO 3505123 <GO>}

Thank you, Joanna.

## Operator

(Operator Instructions) The next question is from John Ransom of Raymond James. Please go ahead.

## Q - John Ransom {BIO 1535724 <GO>}

Hey, good morning team, hope all is well in Houston. Sorry, COVID voice, I guess. So, Eric, or Tom, do you think the -- there -- is it possible there could be a structural pickup in M&A or do you think it's just one of those good years?

## A - Tom Ryan {BIO 3505123 <GO>}

I think, obviously, it could be either, John, because I think our window is probably a 12-month to 18-month window that we can get excited about or not be excited about. I think we've been telling you, we've been excited about 12 months to 18 months out and I still would say that. I tend to believe your first part of the comment, which is, I do think we're in a new era. And I think if you remember, at Investor Day when John presented, we upped our belief as to what we think we'll be able to do on an annualized basis. Not by a significant amount, but I think it gives you an idea that we think, particularly kind of post-COVID and regulatory things that are going on, the aging of the Baby Boomers, the family transitions. So we're -- we believe it's out there and we're out there working hard, and I'd say today we feel very good about the pipeline.

## Q - John Ransom {BIO 1535724 <GO>}

Okay, and I'll probably know the answer to this question, but have you heard anything at all from the FTC?

## A - Eric Tanzberger {BIO 1877182 <GO>}

No. We've not heard anything yet from the -- from the FTC related to our response, which geez, I guess goes back in 2019. Is that right? So yes, we're still waiting to hear any type of response. But again, I just want to reiterate we continue on their main issue to have different levels of pricing that are out there and testing it in different ways. And we're probably going to be ahead of the curve. And we don't necessarily think whatever happens is going to really have a material effect, John, on the long-term health of this business.

## Q - John Ransom {BIO 1535724 <GO>}

And then I know you've done a little bit of this, but is there a future where you do a higher number of de novos than -- than what you're doing now and would it ever move the needle?

## A - Eric Tanzberger {BIO 1877182 <GO>}

I mean, it's possible. You know the de novos are going to have, as we all know, just by stating the obvious, just a slightly lesser term because you're kind of building up EBITDA for the first two or three years as you're building the brand new business. So it's always nicer to be able to go in and not only have well-established EBITDA streams, have well-established businesses, and most importantly, partnering with the management teams and the owners that are in place with some of the wonderful businesses that we just purchased, for example, in the last year alone.

Ultimately, that's just an advantageous effect and with us having only 15% to 16% market share, and call the entire consolidation universe kind of in the 20% range, I just think that there continues to be opportunity out there subject to other market conditions, John, that acquisitions are just going to continue to be a little bit more lucrative. That being said, we've continued to ramp up the de novo spend and we'll continue to do that as well.

## Q - John Ransom {BIO 1535724 <GO>}

Okay, and then just the -- well, never mind, I forgot my question, it's probably getting old. Thanks guys. Appreciate the time.

## A - Tom Ryan {BIO 3505123 <GO>}

Thanks, John.

## Operator

The next question is from Scott Schneeberger of Oppenheimer. Please go ahead.

## Q - Scott Schneeberger {BIO 5302695 <GO>}

Thanks very much. Good morning all. I -- just following up on John's question on M&A, Eric, you mentioned closing something after the end of second quarter. Just curious on the

West Coast and then this allusion to kind of -- to being a strong year in M&A, could you give us a sense of how large that acquisition is that you already closed?

## A - Eric Tanzberger {BIO 1877182 <GO>}

The acquisition that we closed was not a tremendously large acquisition. It was less than $10 million of the spend. What we are talking about in terms of the excitement is some things that are in the pipeline right now that we expect to close that we're very excited about. So more to come on that, Scott.

## Q - Scott Schneeberger {BIO 5302695 <GO>}

Thanks. Appreciate that. I came on a little bit late, my apologies if this has been covered but funeral pricing growth remains pretty strong and I'm just curious how inflation works into that. And when I came on, I think you said something about flowers and ancillary services being soft and that's the part I missed, which flies contrary to the strength in the numbers. So could you just elaborate on -- I guess the way to address it is, going forward, how do you see funeral pricing growth? Is that going to step up to cover costs or is that something that -- that may just -- a steady state from here or even go backwards? Thanks.

## A - Tom Ryan {BIO 3505123 <GO>}

Scott, I think we do believe we can pass along inflationary costs in a standard thing, and what you missed earlier, we talked about a few things that are happening differently. If you recall with COVID, especially initially, we saw a real decline in, I'd say, the full service funeral, and part of that was because of lockdown, access to vaccines, all those types of things. So people were doing smaller ceremonies, having smaller rooms or no rooms, not buying a lot of flowers or catering. What we're seeing is a robust reawakening of all that, and so you think about what's going on now, one of the strategies that we were already putting into place is upgrading a lot of our facilities to have some differential opportunities for, let's say, facility charges.

So as you go into a place, you can get the premium room in one pricing, get the middle room or the lower room. We're seeing a lot of people buying up into that premium room. We're seeing a lot of people buying more flowers, more catering for their specific services. We've done an incredibly good job, our teams, of working on what I'll call third-party flower sales. So you think about the website, so obviously, we sold a lot of flowers to the family, but the friends and family, they go to the Obituary, click on. We're selling more and more flowers through our partnership there and that too is driving -- all of these pieces are working together to drive differential average.

And then at the same time, we believe we can pass along all the inflationary pricing. Now the one thing that puts pressure on pricing every year is that cremation exchange, and we anticipate that to continue. That's probably going to be a bit of a headwind. One unique thing I noticed about this quarter and it's so immaterial for us compared to others, but I thought about it as I looked at Colgate and Procter & Gamble, we're seeing, believe it or not, even through Canada because of the strong dollar, the Canadian dollar conversion is probably a bigger impact on us than -- or as big an impact as cremation mix when you think about average. The nice thing is you convert the cost into dollars too. So it really doesn't hurt till it drops to the bottom line. So we feel good about pricing and we will pass along inflationary, and want to continue to drive more robust celebrations and while utilizing our great and improving facilities, and combine that with catering flowers and other things that make a celebration a lot special.

## Q - Scott Schneeberger {BIO 5302695 <GO>}

Thanks, I appreciate that. And just quick answer if you already covered it, but it's down in the release, the cremation rate ticked up a little bit in the quarter, just comments on that sustainability or if that was a blip? Thanks.

## A - Tom Ryan {BIO 3505123 <GO>}

Yes, I think, Scott, if you remember, we saw a bit of the cremation rate back up last year and we even saw a little bit of it in the first quarter and we always thought the trend pre-COVID was 100 basis points to 150 basis points a year. We went to less than 100 basis points, I think it was, for many quarters last year. So I think you're just seeing a little bit of a reversion to the mean. It's 170 this quarter, I wouldn't get excited about that, but I do think we anticipate getting back to that annual trend of 100 to 150. And our excitement is we have so much more to offer to a cremation customer today and we think in the future. That's a real opportunity for what is now 55% of our customers. So we're just thinking about how can we do more, how can we serve them better and get excited about it.

## Q - Scott Schneeberger {BIO 5302695 <GO>}

Understood, Tom. Thanks. And just one last one and it's kind of a -- I think a good overview was provided of -- from Joanna's questions with regard to cemetery preneed. But if I could just summarize, and you could add a little color on this, we saw a slowdown in the second quarter, maybe a little bit more than you expected. Sounds like it was a bit of the consumer, and maybe just the way, and maybe some unique items, but you still sound confident in achieving, let's call it flattish to slightly positive for the full year in preneed cemetery.

Is it because you just -- how are your leads looking? What gives you that confidence? And any commentary as to the cadence of second half of this year and next year of preneed cemetery? Because I think you're trying to smooth it pretty well. Just want to understand how comfortable you feel on handling the reversion from a potential pull-forward. Thanks.

## A - Tom Ryan {BIO 3505123 <GO>}

Yes. No, I think we still feel very good. And so, to answer, there's a lot of questions, Scott, but I'll try to summarize. So let's break it down. When you think about the consumer right now, we're still seeing a very healthy, I'll call it high-end consumer. So large sales have hung in there even with the stock markets being down in the first half of the year, we got a little bump back in July, hopefully that's there, so the confidence is there.

I think the real issue for us -- and by the way, the average sale even outside of that is hanging in there very good too. So we're really talking about is what's happening with velocity. Well, I'll tell you, from a leads perspective, we're still doing great. We're still seeing a significant amount of leads, and the problem we've had, at least temporarily, is are those appointments holding. People are -- rescind an appointment and somebody cancels or because they're going on vacation, or they got something else to do or they got their gas bill and go, oh shit, I'm not going to do that. So we believe there is a little bit of inflation, a little bit of distraction, because they have other things to do.

The other thing that I mentioned to you is we have seen an outbreak of COVID amongst consumers, and probably is -- again, it's not as deadly a COVID but still people are sick and you're not going to take an appointment or our counselor can't go back and follow up. So our belief is, as we fight through this, our counselors will get back, these employment rates will hold better. Our close rates are really good, so absent inflationary problems, costs, that people may not want to pull the trigger, we still feel very good because the leads are there, our counselors are very effective. We actually believe we're going to have more leads.

So I continue to think things are good, and the only thing I'd point out, and this isn't news to you guys because you read the news like I do, inflation has crept in and if you're a monthly, if you're going to buy over 36 months and you are sitting down with your budget, you may be saying right now, wow, I got to cover the gas bill and so maybe I'll put this off. And I think our belief is if that subsides, people are going to get back in the game and there'll be an opportunity for us to really go back out the sales channel.

## Q - Scott Schneeberger {BIO 5302695 <GO>}

Got it. Thanks, Tom, I appreciate that summary.

## A - Tom Ryan {BIO 3505123 <GO>}

Thanks, Scott.

## Operator

The next question is from AJ Rice of Credit Suisse. Please go ahead.

## Q - AJ Rice

Hi, everybody. Just to make sure I know we're sort of approaching normalcy, would you say COVID-related cases this month are sort of -- are this quarter sort of where you think they're going to settle down? Or you still feel like that's somewhat elevated relative to where things will shake out? I know you've talked about it being down 50 million year-over-year, I think, if I got that right.

## A - Tom Ryan {BIO 3505123 <GO>}

AJ, I think that COVID cases on a national basis I think now are like 300 if I remember right, 300 deaths a day. I would expect that that's probably going to continue for some time. It's very low relative to the periods of COVID, but it's just not material to our numbers. So like we tried to point out at Investor Day, I think we're experiencing -- we're servicing elevated numbers of consumers. And you say, okay, what is that, Tom? Well, we've mentioned a little bit. We think there's still excess deaths. We think we can correlate it with lack of healthcare, people probably drinking too much, smoking too must, driving too fast, depression, access to mental health.

The other thing that we see, and this is kind of a -- it's tough because it isn't perfect data, but we are seeing what we believe are market share gains and really kind of across the board, but probably more acutely in the West. And as we look at states like Arizona, Nevada, Colorado, California, we appear to be gaining a decent amount of share in those markets. So I think those are the reasons why we sit here and say, yes, COVID is not going to be -- have any impact, but we think we've probably got deeper market share penetrations combined with what we believe are excess deaths that will continue to occur in the near-term over the next few years. I hope the country gets healthier, I hope access to healthcare gets better, but the trends don't support that thesis.

## Q - AJ Rice

And for some time there's been discussion about your emphasis on pre-arranged funerals. As that book matures and you started really ramping that up post the credit crisis, that that would drive some market share gains. Is that what you're seeing or is it something else that you think is driving those market share gains?

## A - Tom Ryan {BIO 3505123 <GO>}

I think that contributes to it, AJ, because one of the things, if you think about the markets that I just mentioned, they are high combination facility markets. So as you think about Colorado, Arizona, so more -- again, more specifically by Phoenix, Denver, LA, really all up and down California, and you look at those places, Las Vegas, Nevada, those are places where we're really not going to hit the ball hard. Where we've got great cemetery, we've got great sales forces, and do believe that they have penetrated those markets. So, surely a contributing factor, not all of it, but that's why strategically we've set out to do that thing.

## Q - AJ Rice

Okay. Any updated thoughts on, you guys have been good throughout this, to try to -- you have a sense of how much pull-forward was sort of near-term and how much is more long-term? Have you revisited that as time is passing in any way? And any updated thoughts on what that pull-forward of COVID deaths implies for the next number of years?

## A - Tom Ryan {BIO 3505123 <GO>}

Well, Eric's got a medical degree and he's a professional demographer. I'm going to pass that to him. He's been studying this, AJ.

## A - Eric Tanzberger {BIO 1877182 <GO>}

Yes, AJ, it's really no other data is what I -- what the short answer is, that we talked about at Investor Day. We put some numbers out there that we thought they were somewhere in the range of 15,000-ish cases that were pull-forward in 2022, probably the same in '23 and then it really drops off. So as we've gone in and tried to look at it a little bit and decide how far off are we, the answer is probably, we're pretty close to those estimates. At least for the visibility that we have now. So, no change, no material change to really report is the answer.

## Q - AJ Rice

Okay. And obviously you commented on the acquisition pipeline and your optimism about that. Is there anything that you're seeing? I know it ebbs and flows but is there anything that seems to be driving a bit of an uptick in activity and any comments you can make on whether pricing on potential deals is relatively stable or moving around or competition for deals, if there is any?

## A - Tom Ryan {BIO 3505123 <GO>}

Yes. So I think first of all, we do think more people are out there trying to sell. I think it's a combination of the aging of the owners without a succession plan, because most of these are owned by Baby Boomers, right? So every year, they get a little bit more -- I'd like to have more free time and have a liquidity event. So I think that's just a natural backdrop that we're working against. Combine that with COVID which has been kind of a two-and-a-half, three-year frenzy and people having to work really hard, people having to deal with staffing issues. So I think that puts a lot of pressure on a reasons to sell.

As far as pricing goes, I think we've held pretty good. I'd say it's probably, people come in with an expectation, AJ, as you can imagine, here's my 2021 numbers, I'd like to be paid for that. Our opinion is those aren't sustainable numbers, and so we try to realistically say, what's the pace of this business. And -- but that's obviously going to start a conversation at a higher expectation. So I would say it's not materially different. But I do think that's part of the process and at the end, I think we get to a good answer. So as far as the competitors go, it's really the same groups of people that we see out there, I'll say a lot of new entrants. But if you roll back the clock five years, there's probably a little more activity, a little more competitive pressures as you think about the acquisition pipeline. John do you disagree or -- John? No? Okay. So you get that. John agrees with me, that's rare, so write that down.

## Q - AJ Rice

Okay. Thanks a lot.

## A - Tom Ryan {BIO 3505123 <GO>}

Thank you.

## Operator

This concludes our question-and-answer session. I would like to turn the conference back over to SCI management for closing remarks.

## A - Tom Ryan {BIO 3505123 <GO>}

Thank you everybody for being on the call today. We appreciate you and we look forward to speaking to you again, I believe, in late October, early November. Talk to you soon.

## Operator

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.