



Healthcare Services Group (HCSG)

Updated August 21st, 2022, by Tiago Dias

Key Metrics

| | | | | | |
|-----------------------------|------|--|------|----------------------------------|------------|
| Current Price: | \$15 | 5 Year CAGR Estimate: | 7.0% | Market Cap: | \$1.1 B |
| Fair Value Price: | \$15 | 5 Year Growth Estimate: | 2.0% | Ex-Dividend Date: | 08/19/2022 |
| % Fair Value: | 100% | 5 Year Valuation Multiple Estimate: | 0.0% | Dividend Payment Date: | 09/23/2022 |
| Dividend Yield: | 5.7% | 5 Year Price Target | \$17 | Years Of Dividend Growth: | 19 |
| Dividend Risk Score: | C | Retirement Suitability Score: | B | Rating: | Hold |

Overview & Current Events

Healthcare Services Group (HCSG), founded in 1976, is a Pennsylvania corporation that provides management, administrative and operating expertise and services to the housekeeping, laundry, linen, facility maintenance and dietary service departments of healthcare facilities throughout the United States. With a dividend that has grown on a yearly basis since 2003, this \$1.1 billion market cap company generates approximately \$1.7 billion in annual revenue. The company reported Q2 2022 earnings on July 20th, 2022, and declared a quarterly dividend of \$0.21375 per share, the 76th consecutive increase since 2003. With earnings of \$0.09 per share, compared to \$0.13 in last year's quarter, this dividend is not well covered by the companies' earnings. Revenue equaled \$424 million versus \$398 million in the year ago period. Inflation has harmed the company over the past year, with cost of services provided being higher than historical norms, though the management team is working to restructure the companies notes receivable with certain clients, altering the timing of collections with others, and even exercising termination rights if needed.

Growth on a Per-Share Basis

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|---------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$0.65 | \$0.67 | \$0.31 | \$0.80 | \$1.05 | \$1.19 | \$1.12 | \$0.87 | \$1.32 | \$0.61 | \$1.00 | \$1.10 |
| DPS | \$0.65 | \$0.67 | \$0.69 | \$0.71 | \$0.73 | \$0.75 | \$0.77 | \$0.79 | \$0.81 | \$0.83 | \$0.86 | \$0.90 |
| Shares | 68 | 70 | 71 | 73 | 73 | 74 | 75 | 75 | 75 | 75 | 76 | 80 |

Earnings per share have followed revenue throughout the period, with somewhat steady growth up until 2018. The 2019 numbers suffered as a result of decreased revenue and margins due to business model changes. These changes have continued since and resulted in noticeably lower revenue and profit margins.

The company is a low margin services business, and as a result their business is heavily affected by the impact that wages and inflation have on their profit margins. This is particularly noticeable when comparing a low inflation year like 2020, with high inflation years like 2021 and 2022.

The service agreements the company holds with its clients can be modified, and the management team is confident that doing so would help the company bring back its operational margins to its historical averages. As such, we expect earnings-per-share to rise to around \$1 in late 2022.

This should provide some favorable tailwinds to an otherwise unremarkable business, though it is not likely that earnings-per-share will come back to 2017/2018/2020 highs without some yet unseen catalyst to increase revenue. It's this lack of a revenue growth catalyst that means our estimates for 2027 are a conservative \$1.10 earnings per share, in line with our 5-year growth estimate of 2% annually.

Valuation Analysis

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | Now | 2027 |
|------------------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| Avg. P/E | 29.2 | 32.8 | 83.9 | 37.5 | 32.4 | 41.2 | 34.8 | 27.6 | 23.5 | 29.5 | 15.0 | 15.0 |
| Avg. Yld. | 3.4% | 3.1% | 2.7% | 2.4% | 2.2% | 1.5% | 2.0% | 3.3% | 2.6% | 4.6% | 5.7% | 5.5% |

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Healthcare Services Group (HCSG)

Updated August 21st, 2022, by Tiago Dias

Investors have historically been willing to pay a premium for Healthcare Services Group, likely as a result of historically high revenue growth. However, with revenue growth, and subsequent earnings and margin compression since 2018 it's clear that investors are beginning to re-rate the company to an earnings multiple that is more in line with the company's lackluster prospects. This has resulted in an historically low P/E multiple of 15, in line with the market average.

While we believe the company can maintain its dividend growth policy, we are forecasting just 1% annual dividend increases from this point. In turn, we expect the payout ratio to remain around 80% of earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 100% | 100% | 223% | 89% | 70% | 63% | 69% | 91% | 62% | 136% | 86% | 82% |

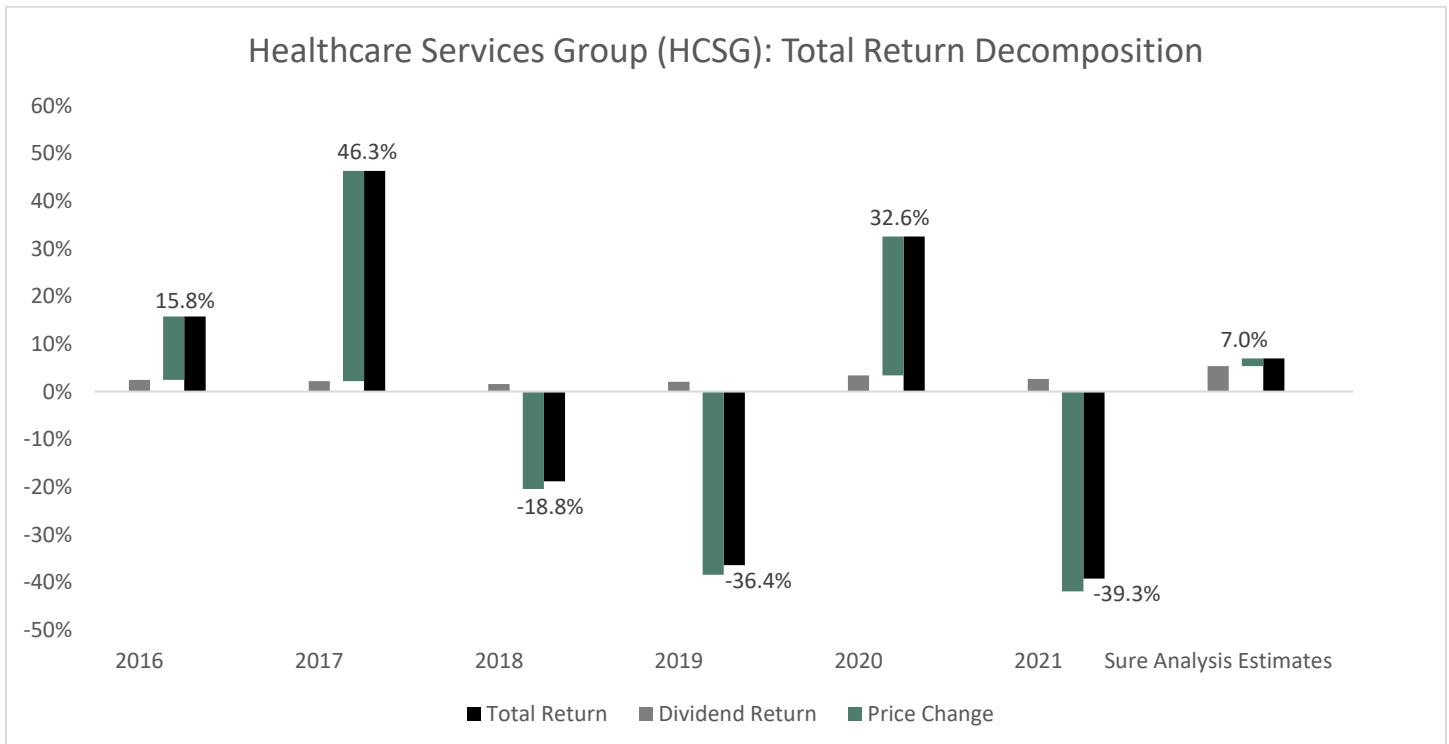
Operationally speaking, the company is a low margin services business in a highly competitive industry without any significant competitive advantage against other similar businesses, or even their clients inhouse housekeeping departments.

The almost total lack of debt as part of their capital structure means that its accounts receivable is more than enough to pay off all its liabilities and is a good indication of the quality of the management team. This lack of debt provides the company with enough stability to survive almost any recession, and is an encouraging sign for the company's dividend, particularly given that it has regularly issued higher dividends than its earnings would be able to support.

Final Thoughts & Recommendation

Healthcare Services Group's five year estimated total return comes in at 6.9% per year, driven by a 5.7% dividend yield and 2% expected earnings growth rate. It's clear that the company is not being priced attractively considering the underlying fundamentals of the business and its dim prospects. Due to the low anticipated returns, the company's shares earn a Hold rating.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



Healthcare Services Group (HCSG)

Updated August 21st, 2022, by Tiago Dias

Income Statement Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | 1,077 | 1,150 | 1,293 | 1,437 | 1,563 | 1,861 | 2,003 | 1,841 | 1,760 | 1,642 |
| Gross Profit | 147 | 155 | 138 | 201 | 223 | 251 | 234 | 228 | 268 | 227 |
| Gross Margin | 13.6% | 13.5% | 10.7% | 14.0% | 14.3% | 13.5% | 11.7% | 12.4% | 15.2% | 13.8% |
| SG&A Exp. | 78 | 89 | 107 | 112 | 104 | 127 | 137 | 150 | 142 | 166 |
| D&A Exp. | 5 | 6 | 7 | 8 | 7 | 9 | 9 | 14 | 14 | 15 |
| Operating Profit | 69 | 66 | 31 | 89 | 119 | 124 | 98 | 78 | 126 | 60 |
| Op. Margin | 6.4% | 5.7% | 2.4% | 6.2% | 7.6% | 6.7% | 4.9% | 4.2% | 7.2% | 3.7% |
| Net Profit | 44 | 47 | 22 | 58 | 77 | 88 | 84 | 65 | 99 | 46 |
| Net Margin | 4.1% | 4.1% | 1.7% | 4.0% | 5.0% | 4.7% | 4.2% | 3.5% | 5.6% | 2.8% |
| Free Cash Flow | 57 | 28 | 52 | 58 | 36 | 2 | 75 | 89 | 213 | 31 |
| Income Tax | 26 | 19 | 10 | 32 | 43 | 45 | 16 | 21 | 31 | 16 |

Balance Sheet Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|-------------------------------|------|------|------|------|------|------|------|------|------|------|
| Total Assets | 331 | 425 | 470 | 481 | 528 | 676 | 693 | 723 | 785 | 778 |
| Cash & Equivalents | 69 | 64 | 75 | 33 | 24 | 10 | 26 | 27 | 139 | 71 |
| Acc. Receivable | 140 | 189 | 198 | 215 | 271 | 379 | 342 | 341 | 255 | 293 |
| Inventories | 29 | 32 | 35 | 36 | 38 | 42 | 41 | 37 | 32 | 26 |
| Goodwill & Int. | 22 | 64 | 65 | 62 | 59 | 82 | 78 | 73 | 69 | 96 |
| Total Liabilities | 102 | 140 | 194 | 184 | 190 | 276 | 252 | 262 | 305 | 325 |
| Accounts Payable | 23 | 44 | 44 | 41 | 43 | 74 | 61 | 54 | 52 | 64 |
| Long-Term Debt | --- | --- | --- | --- | --- | 35 | 30 | 10 | --- | --- |
| Total Equity | 230 | 285 | 276 | 296 | 339 | 400 | 441 | 460 | 480 | 453 |
| LTD/E Ratio | --- | --- | --- | --- | --- | 0.09 | 0.07 | 0.02 | --- | --- |

Profitability & Per Share Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return on Assets | 14.2% | 12.5% | 4.9% | 12.2% | 15.3% | 14.7% | 12.2% | 9.1% | 13.1% | 5.9% |
| Return on Equity | 19.8% | 18.3% | 7.8% | 20.3% | 24.4% | 23.9% | 19.9% | 14.3% | 21.0% | 9.8% |
| ROIC | 19.8% | 18.3% | 7.8% | 20.3% | 24.4% | 22.8% | 18.4% | 13.7% | 20.8% | 9.8% |
| Shares Out. | 68 | 70 | 71 | 73 | 73 | 74 | 75 | 75 | 75 | 75 |
| Revenue/Share | 15.73 | 16.42 | 18.13 | 19.82 | 21.27 | 25.03 | 26.84 | 24.68 | 23.54 | 21.90 |
| FCF/Share | 0.83 | 0.41 | 0.73 | 0.80 | 0.49 | 0.03 | 1.01 | 1.20 | 2.85 | 0.42 |

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.