Primo Water Q2 2024 Earnings Call Transcript

August 8th, 2024

Company Participants

- Jon Kathol, Vice President of Investor Relations
- David Hass, Chief Financial Officer
- Robbert Rietbroek, Chief Executive Officer

Operator

Good morning. My name is Lara, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Primo Water Corporation, second quarter 2024 earnings conference call. All lines have been placed on mute to prevent any background noise. Should you require operator assistance during the call, please press *0. I'll now turn the call over to Jon Kathol, Vice President of Investor Relations.

Jon Kathol

Welcome to Primo Water Corporation, Second Quarter 2024 Earnings Conference Call. All participants are currently in listen only mode. The call is being webcast live on Primo Water's website at primowatercorp.com and will be available there for playback.

This conference call contains forward looking statements regarding the Company's future financial and operational performance, the anticipated benefits and strategic rationale of the BlueTriton transaction, including estimated synergies and capital expenditure rates, the ability of Primo Water to complete the transaction on terms agreed or at all, the expected timing of the completed transaction, receipt of regulatory court and Stock Exchange approvals and other statements that are not historical facts.

These statements should be considered in connection with cautionary statements and disclaimers contained in the safe harbor statements in this morning's earnings press release and the Company's annual report on form 10-K and quarterly reports on Form 10-Q, and other filings with securities regulators. The Company's actual performance could differ materially from these statements, and the Company undertakes no duty to update these forward-looking statements, except as expressly required by applicable law.

A reconciliation of any non-GAAP financial measures discussed during the call with the most comparable measures in accordance with GAAP, when the data is capable of being estimated, is included in the Company second quarter earnings announcement released earlier this morning or on the investor relations section of the Company's website at primowatercorp.com. In addition to slides accompanying today's webcast to assist you throughout our discussion, we have included a copy of the presentation in a supplemental earnings deck on our website.

I'm accompanied by Robbert Rietbroek, Primo Water's Chief Executive Officer, and David Hass, Chief Financial Officer. As previously announced, we will not be taking live questions from analysts or investors during this call. Instead, the most pertinent questions have been selected and will be addressed by our management team during today's call. Today's scripted comments will focus on Primo Water's current standalone results from continuing operations, questions and updates related to the proposed merger with BlueTriton brands will be addressed in the moderated question and answer session on this call. With that, I will now turn the call over to Robbert.

Robbert Rietbroek
Thank you Jon and good morning everyone. Since the beginning of this year, our team embraced a new strategy that includes a relentless focus on customer centric initiatives, must win priorities, as well as a commercial and growth mindset, leveraging our portfolio of hydration solutions.

Our must wins are focused on delivering a superior customer experience, positioning ourselves as a partner of choice to retail partners and other key stakeholders and operational excellence. Our brand portfolio is driving sustainable growth, and results are strong.

Our second quarter results showed continued strength across the Business and Organization, with broad based and balanced growth across channels, strong progress against priorities, unit growth combined with pricing, enabling us to expand margins and generate a higher rate of free cash flow, while delivering against sustainability targets. Total revenue of $485 million increased 7.6%, consisting of volume growth of 3.1% and pricing growth of 4.5%.

Revenue gains were driven by organic growth of 6.6%, demonstrating the health of our consumer and category as well as our strength across our brands and water solutions offerings in the current economic environment.

Adjusted EBITDA was $113 million, up 15% versus the prior year, and increasing at nearly twice the rate of revenue growth. The resulting adjusted EBITDA margin was 23.3% which gives us confidence in our full year margin expansion. Both revenue and adjusted EBITDA exceeded the high end of our guidance issued last quarter.

David will discuss more of the details of the quarter in a moment, but the results are a direct reflection of our associates and their commitment to our customers. I would like to publicly recognize and thank them for embracing our must win priorities and remaining frontline focused while staying dedicated to growing the business profitably.

From a macroeconomic perspective, demand for our water solutions is strong, and consumers continue to prioritize healthier lifestyles and focus on hydration. We offer high quality drinking water solutions to meet the consumer demand however they choose to hydrate.

We continue to see the growth potential as a pure-play water Company in the large, highly fragmented and growing North America water category. High quality drinking water has universal appeal and is a solution for all day parts and usage occasions.

Our split between residential and commercial customer base remains approximately 50/50, ensuring a healthy balance of revenue sources. As a beverage company, compared to the broader beverage category, we are pleased that we continue to grow revenue in both volume and price.

Furthermore, our current and future business opportunities benefit from additional tailwinds, including growing environmental concerns. Our extensive water resources ensure availability and are reinforced by our dedication to responsible water source stewardship.

With that, let us discuss the specific progress of each of our must win priorities that I identified upon arriving earlier this year. The first must win is to provide a superior customer experience with the goal to yield net organic growth and units, or gallons, consumed across our water portfolio. We are focused on acquiring and maintaining high value customers and driving annual gallon growth.

Consumers can select our products from multiple price tiers, from a value price of 50 cents per gallon for water sold at a refill station, all the way up to our super premium Mountain Valley Spring water, delivered in multi format, glass, PT and aluminum bottles direct to their door or, sold at retail and various on-premise locations. Our increased focus on Mountain Valley, which I spoke about last quarter, continues to deliver impressive results.

During the second quarter, we increased our Mountain Valley retail revenue by approximately 87% over the prior year.

We are off to an impressive start with the launch of our convenient nine pack single serve 16-ounce aluminum bottles, which began sale in food stores throughout the country and to our water direct customers in Q2. Mountain Valley is already a leading brand of spring water sold in a natural foods channel, and we continue to see high levels of Mountain Valley demand for our five gallon, two-and-a-half-gallon retail and on premise, multi serve and single use products. We continue to scale operations in support of the Mountain Valley growth and are currently running all three of our glass bottling lines 24/7.

Looking ahead to our broader portfolio, we have planned customer recruitment marketing programs like “refer a friend”, “movers” and “returning customers”, that will include a targeted media campaign, and frictionless end to end customer experience where it's easy to do business with us. We are consistently enhancing various consumer touch points to improve their experience.

This quarter, traffic to our digital assets was up 29% as we upgraded the “My Water Plus” app with the fresh design, enhanced features, and launched improvement store water.com quick shop features to streamline the customer shop-to-cart journey, particularly when engaging with our promotions, and enabled easier access to customer support through our chat feature, now available six days a week.

By increasing the coverage of our Customer Experience Center, we had over 30,000 interactions with customers via our chat functionality, with the focus on our quality of service and rapid request resolution. The initial reaction to our increased customer experience efforts is encouraging. Our Google Business rating has improved 8% year over year, and our net promoter scores have improved 12% from the prior year.

The second must win is to be the preferred water solutions partner. We meet the end consumer across numerous channels, like direct-to-consumer delivery or through one of our retail partners, with our exchange locations or refill stations. We have an offering to meet each of our customers’ needs and budget, or what we call “water your way”.

Customer and volume growth starts with increasing the number of customers and locations in water direct, exchange, refill, and the sale of water dispensers at retail, which drives connectivity across our portfolio of water solutions. During the second quarter, we were able to secure additional display racks with certain major retail stores to support capacity in our exchange channel, our focus on filling white space gaps and increasing capacity and in stocks is having a noticeable effect by driving double digit revenue growth in the exchange business.

Increase in customers and locations will drive future volume growth. As evidence of this future growth, we were recently awarded an agreement to place up to 1000 incremental refill machines with the large chain of convenience stores in the US. Placement of these machines will begin taking place in the remainder of 2024 and well into 2025.

The concept of partnering stretches across all aspects of our business, including associates, suppliers, customers and current and potential share owners. It begins with our associates, whose dedication is evident in every aspect of their efforts.

Ensuring a safe environment is our top priority and is essential for our associates to thrive, and we are committed to enhancing our workplaces, upgrading offices, locker rooms, break areas and parking facilities, as well as production and distribution areas. Associate safety at work, as well as in the home, is being fostered to the Q2 launch of the “100 Days of Safety” summer program aimed at raising awareness for summer safety best practices, but also rewarding associates for adopting a safety mindset. The program rollout has yielded promising results in reported incidents and overall associate retention and engagement. Community involvement is a key element of our culture as our associates live in the areas we serve, and are passionate about the products and services we provide.

One example of our community involvement includes providing support in times of need, like supplying water in times of natural disasters, like the wildfires and hurricanes across several states, as well as during municipal water emergencies. Last quarter, we also went above and beyond providing our products and services in times of need by investing our time in the betterment of our communities. We had the pleasure of co-hosting a community cleanup recently with the city of Hot Springs, parks and trails, the home of our Mountain Valley brand. We embrace our partnerships, and our customer base spans across all types of retail, including mass merchandisers, club stores, DIY and e-commerce, with top tier retailers like Walmart, Costco, Home Depot, Lowe's and prominent grocery chains throughout North America.

I continue to engage with these world class retailers and top-to-top meetings, and I found a strong desire on their part to drive more traffic to their stores and websites with our dispensers and water accessories such as the rolling water cooler available on select retailer sites and water.com, exchange and refill stations, as well as Mountain Valley Spring water.

David and I, once again, had numerous and extensive interactions with investors and analysts in the second quarter. These themes included an appreciation for our North American focused business model, our growth algorithm, free cash flow generation and conversion, progress on the sale of the European and Israeli assets, an appreciation for our strong balance sheet and low leverage, how we plan to deploy capital in the coming quarters, and of course, a review of our planned merger with BlueTriton Brands.

I would like to extend my personal gratitude to our stakeholders for their high level of engagement. By maintaining, strengthening and enhancing these partnerships, we can achieve even greater success together.

The third must win is operational excellence, specifically ensuring that we have an optimized organizational structure and operating systems to guarantee our associate safety and wellbeing deliver the highest quality product and service to our valued customers and scale efficiently as we continue to grow.

During the second quarter, we began implementing six and seven-day delivery schedules as we moved into our traditionally busy period of the summer. We were able to increase our on time and full rate to 94% in our water direct channel for the second quarter, with positive feedback from our exchange customers on the strengthened holiday service support. Our refill channel had machine uptime of 98%, an increase over last quarter, and our time to address service calls improved by one and a half days versus last quarter.

Throughout our operations, we are driving integrated business processes. During the second quarter, we increased our revenue per route by 5%, and units per route per day by 2%, an indication of improved asset utilization, route density and positive volume and pricing improvement mix. The same principles are now being employed in the optimization of our refill routes, enabling us to extract more value from our team of technicians and service providers.

We remain focused on strategic CapEx investments that deliver high returns. The installation of the new high efficiency production lines continues, and we brought our effort up in Sylvania production line online during the quarter. The performances of the high efficiency line installations are driving a reduction of water waste at the filler and can nearly double the output capacity of the bottling line. We are utilizing advanced robotics to assist some of the more strenuous aspects of our plant and distribution functions, ultimately freeing up our associates to focus on the quality aspects of their roles.

The team is on track to deliver the previously announced business optimization program that will enhance our productivity and lower our overall cost to serve while continuing to offer customers an exceptional experience. We remain committed to the annual run rate savings of $20 million by year end 2024 and David will speak to the achievements this quarter and the progress to our full year goals.

From a sustainability perspective, we strive to source and process responsibly, to protect the planet we inhabit. We will continue to implement our environmental strategy that is focused on sourcing water responsibly, converting our fleets to more eco-friendly propane; reusing, refilling and recycling of our plastic bottles and increasing the use of glass and aluminum as part of our product offering.
We carefully monitor our withdrawal rates, and we use less than 25% of the permitted withdrawal limits, ensuring the long term viability of our 100 water sources, which include 26 of our own wells and springs.

We will detail these results and improvements in our 2023 sustainability report, which will be released later this quarter. We have a clear plan to deliver growth and profitability with the favorable balance of volume and pricing. Our unique combination of associates, assets and resources are capable of delivering strong results that benefit all our stakeholders. We are well positioned for future success.

Before I turn the call over to David to review our financial results in greater detail and provide our third quarter and full year 2024 outlook, I would like to once again, thank all our Primo Water associates for their support and contribution to the excellent performance of the business. With that, I will now turn the call over to David.

David Hass
Thanks, Robbert. As a reminder, at the end of 2023 we disposed of a significant portion of our international assets, and thus our financial results discussed today are for continuing operations only. We are not covering discontinued operations unless otherwise noted.

The second quarter results of our continuing operations included revenue increasing 7.6% to $485 million, adjusted EBITDA increasing 15% to $113 million with adjusted EBITDA margins of 23.3%.

All metrics exceeded the high end of our most recent guidance. Within the 7.6% revenue growth, approximately 6.6, or approximately $29.8 million, came from organic growth activity with the balance 1% or approximately $4.6 million coming from inorganic or acquired sources.

Primo Water's definition of inorganic contribution includes any acquired businesses that were closed less than 12 months ago. After 12 months, any acquired business becomes part of our normal contribution base.

Separately, the 7.6% revenue growth, irrespective of organic or acquired means, can be split into approximately 3.1% related to volume activity and approximately 4.5% related to pricing activity.

Volume contribution in this case comes from both new customer additions or additional gallons consumed from existing customers, or additional retail traffic in our exchange or refill businesses, where actual customer counts are not directly known. Volume activity in the quarter was strong across all of our water solutions, indicating strength in our bulk oriented offering, as well as the complementary nature of our different water channels.

We believe that volume across our water solutions will continue to be a primary indicator of business health versus overall customer counts. Once again, we have expanded our channel disclosure to break out the price and volume splits for each of the channels versus prior year. A table of the results is included with our supplemental earnings deck.

You will notice that volume gains occurred across each of the water channels and price improved, except for the welcome price decline in water dispensers. Within our channels, we had strong revenue growth of 7% in water directing and exchange and a 12% increase in our water refill and filtration channel. The other water channel, which is primarily the retail and on premise, portion of Mountain Valley premium spring water, was up 87%.

The water dispenser business, representing the sell in of our units to the retailer, declined 21% driven by a decline of 16% from volume and expected lower wholesale prices as the tariff elimination works through our pricing architecture.

On the heels of a very strong first quarter through the first half of 2024, the water dispenser business is up 2%, driven by volume of approximately 15% and offset by pricing of -13%. The other channel decline is reflective of our remaining non-core office coffee services, which is not a point of emphasis in our current model.

Water dispensers sell through, or those items sold from the retailer to the end customer, was approximately 260,000 units in the quarter, up approximately 4%. As a reminder, our business model includes two approaches of selling the water dispenser, the rental of the water dispenser to residential and commercial customers in our water direct business and the sale of water dispensers through our retail partners and online.

Both approaches enable growth in water solutions and contribute to our predictable and recurring revenue growth. We have been particularly focused on growth with our brick-and-mortar retail partners, where we have greater visibility into the connectivity to our water solutions, and higher connectivity compared to e-commerce channels.

As discussed in previous calls, our water dispenser category was previously under a 25% import tariff, but was reclassified last year, and a refund process from the US government was initiated. When we receive funds, we record them in the same manner as the original transactions.

During Q2, we did not receive any refunds, reflecting the inconsistent nature of the government refund process when including last year's payments. Cumulatively through the second quarter of 2024 we have received approximately $10.8 million. We remain confident that refunds will be received, but we cannot predict the timing of receipt.

As we look further into the operational metrics, and as Robbert mentioned earlier, our commitment to improving the customer experience continues to result in improved on time in full or “OTIF” rates.

The ability to serve our customers in the most efficient manner possible is a critical driver of both our short and long term profitability and our automated Route Optimization, or “ARO” tool, continues to yield efficiencies.

In the U.S., units per route per day increased approximately 2% compared to Q2 of 2023 and revenue per route increased more than 5% compared to Q2 of 2023. Our scale and leverage continue to improve as we service more customers with higher volume per route.

Additionally, water direct customer retention increased to approximately 86% an increase versus the end of last year and the second quarter of 2023.

Shifting to our balance sheet and cash flows. Our net leverage ratio at the end of the second quarter on a trailing 12 month basis stood at approximately 1.6 times our adjusted EBITDA, a 50 basis point improvement from year end 2023.

Similarly, our liquidity remains strong, with approximately $603 million of cash on the balance sheet, approximately $615.5 million when considering the cash within our discontinued operations and a fully unused cash flow revolver.

Specific to our cash flow revolver, we recently extended the maturity of our revolver to September 2026 which will allow us time to establish the proper capital support financing for NewCo once the merger is completed.

In the quarter, we paid approximately $21.4 million of interest net of interest income. On a full year basis, while we will be a net interest expense payer, we are quite pleased with both the low interest rate carried on our senior notes and our ability to generate interest income in today's yield environment.

During the second quarter, we completed the sale of Aimia foods, our UK Food and Drink business, for $75.5 million, approximately $91 million when including dividends extracted from the business.

After the close of Q2 we successfully completed the sale of our Portugal business for $19.2 million. Due to the timing of the Portugal sale, the funds are not reflected in our Q2 balance sheet.

We remain on target to complete the sale of the businesses in Israel and the UK by year end. The Israel process is being run by an investment bank, and interest levels are strong. Our adjusted free cash flow results for the second quarter totaled $73 million, a year over year improvement of $34 million.

The improvement was primarily driven by increased earnings, reduced net interest expense, and improved working capital, offset by increased levels of capital expenditures and higher cash taxes due to fewer NOLS as we shift to a net taxpayer relative to prior years. As a reminder, our increase in year over year adjusted free cash flow is different than how that growth contributes to our full year 2024 guidance, which I will discuss in a few minutes.

We are incredibly pleased with the free cash flow momentum on a year-over-year basis. The results for the second quarter reflect a series of receivable improvements and improved inventory levels that began in the second half of last year and are still driving benefit today. As supported in our supplemental earnings deck, in the third quarter of 2023, we posted adjusted free cash flow of $92.7 million in our continuing operations, which was the primary contribution for our full year 2023 results of $157.8 million.

Because of this outsized contribution, as we head into the third quarter of 2024, we expect a more measured outcome per quarter in our free cash flow for the second half of 2024.

In summary, we are pleased with our ability to maintain a high conversion of our adjusted EBITDA into free cash flow, and our 2024 guidance contemplates this outcome.

Once again, as I transition into our 2024 outlook, any forward guidance will strictly be for continuing operations. Discontinued operations will not be covered. To help bridge our 2024 guidance, a table of 2023's financial results for continuing operations by quarter has been provided in the appendix of our supplemental earnings slides.

We are forecasting third quarter revenue guidance to be between $485 million and $495 million. We expect Q3 adjusted EBITDA to be between $115 million and $125 million, with an implied adjusted EBITDA margin of 24.5% at the midpoint. The 24.5% adjusted EBITDA margin represents a 70 basis point improvement from the year ago period.

For the full year 2024 forecast of continuing operations, we are increasing our revenue projection to be projection to be between $1.87 billion and $1.89 billion, with revenue growth at the midpoint of 6.1%.

Similarly, we are increasing our full year 2024 adjusted EBITDA to be between $420 million and $440 million, with an implied adjusted EBITDA margin of 22.9% at the midpoint. The increase in guidance contemplates both the benefit from the strong start in the first half of the year, as well as some balance of your benefit from our business optimization program.

During Q1, we discussed cost reduction activities of approximately $2 million, and during Q2, we took action on another $2 million, bringing the total to $4 million that will be achieved within 2024. This is reflected in our adjusted EBITDA guidance increase.

These savings will annualize out to approximately $8 million on a 2025 run rate basis toward our $20 million goal. We are maintaining the forecast of the 2024 CapEx guidance of approximately 7% of our revenue guidance range, plus an incremental $22.5 million of strategic CapEx. Full year 2024 cash taxes are expected to be approximately $35 million to $45 million, a $5 million increase at the midpoint, driven by an $18 million increase in the midpoint of adjusted EBITDA since our initial guidance on February 22.

The cash tax guidance includes utilization of U.S net operating losses, or NOLs, of which we have approximately $46 million available for use in 2024. We still expect the amount of NOLs available to be approximately $16 million in 2025 and $10 million per year in 2026 through 2029.

For full year 2024, we are revising the midpoint of our net cash interest expense guidance down $5 million from a previous range of approximately $30 million to $50 million to now $25 million to $45 million. The decrease is a result of cash interest earned halfway through the year, as our balance sheet remains strong and our fixed rate capital structure carrying very low interest rates of approximately 4.2% maturing in 2028 and 2029.

Additionally, we will take steps to maximize the interest income yield throughout 2024 but could experience reduced income opportunities if market available rates decline related to any macro, fed, or bank rate environment decisions.

Combining all of these factors along with the core health and cash generation capacity of our business model, we are forecasting adjusted free cash flow from continuing operations of between $180 million and $190 million in 2024.

The $5 million increase at the midpoint is attributed to the free cash flow conversion of the $10 million increase in our adjusted EBITDA guidance. This outlook solidifies our commitment to replace the adjusted free cash flow that was tied to the international assets sold and those held for sale in our discontinued operations. This team should be commended for the speed of achieving this goal.

The following three items have not been included in our 2024 guidance due to the uncertainty in timing with each discrete outcome. First, for the remaining balance of the business optimization program, we remain confident in achieving the $20 million improvement on a 2025 run rate basis. Second, the remaining benefits from the additional tariff refunds outside of the amounts mentioned and received during the quarter due to the uncertain timing of the government refund process. Third, the sale of discontinued operations, which includes our water business in Israel and our water and coffee business in the United Kingdom.

As previously communicated, these businesses will remain in discontinued operations until they are sold. They are actively being marketed and have received interest from several parties.

Prior to the announcement of the merger with BlueTriton, we had repurchased shares of $6.8 million. On a year-to-date basis, we have repurchased shares of $15.9 million. Subsequent to the announcement, we have suspended share repurchases for the interim period until closing. We intend, however, to issue a special dividend of approximately $0.82 per common share to Primo Water shareholders following board approval and setting of the record date and payment date prior to the closing of the merger with BlueTriton.

Recently, our board of directors authorized a quarterly dividend of $0.09 per common share, a 13% increase over last year, which continues our path to the multi-year dividend step-up with an increase in our quarterly dividend per share of $0.01 for the third consecutive year.

In closing, our improved financial profile and flexibility, along with a compelling long-term growth outlook, are a solid foundation for continued success. We are well-positioned for the merger with BlueTriton Brands. With that, I will turn the call back over to Jon for Q&A.

<u>Q&A</u>

Jon Kathol
Thanks, David. As I mentioned earlier, we will not be taking live questions from analysts or investors during this call due to the proposed merger with BlueTriton. Instead, the most instead, the most pertinent questions have been selected and will be addressed by Robbert and David during today's call.

Robbert, the first question is for you. You're a few quarters into your role. How do you view this quarter's performance and what were the key takeaways?

Robbert Rietbroek
Thanks, Jon. In this macro environment and in the broader beverages category, I'm encouraged by our balanced and broad-based results, which includes a combination of volume, pricing, and strength across each of our water channels.

This has enabled us to deliver the 7.6% overall revenue growth, broken down into 3.1% volume and 4.5% price growth. This continues to represent a nice balance that we've experienced over the last few quarters between volume and pricing actions. The majority of revenue growth occurred from organic sources at 6.6% in the quarter, with inorganic contributing 1.0%. Our associates are very focused on our growth agenda.

We continue to deliver on key operating metrics on time, in full, customer retention, and generating organic sales additions, either with customer ads or location expansion in our retail business. While there's always some timing variances quarter to quarter in dispenser results, we again delivered sell-through growth of 4% year over year. Dispenser sell-through remains a key indicator of the connectivity to our water solutions. It also implies continued momentum in future customer ads and increased volumes.

We continue to make progress on business efficiencies, and I would ask David to discuss this in more detail, but overall, balancing the success of our must-win priorities and disciplined cost control while driving productivity is leading to our strong results in the quarter. In summary, our strong second quarter results and continued business momentum provide us with the confidence to increase our full year guidance for revenue, adjusted EBITDA, and free cash flow generation.

Q - Jon Kathol
David, could you provide a bit more detail on the quarter and key takeaways, notably on your free cash flow?

A - David Hass
Sure, Jon, thanks. You know, first, I echo Robbert's view on the strength of our second quarter results.

Importantly, we outperformed the high end of our Q2 guidance for revenue, adjusted EBITDA, margin, and free cash flow generation. This strong performance enables us to increase our annual revenue guidance to be between $1.87 billion and $1.89 billion, a $10 million increase raise at the midpoint.

This now implies a 6% revenue growth rate versus fiscal 2023. We knew heading into 2024 that we had strong momentum from our fourth quarter results. And our strong first half start to fiscal 2024 confirms that momentum is continuing. Gross margin for the quarter increased 110 basis points to 65.6% with improvements driven by volume leverage through our operations, as well as our business optimization efforts taking effect.

Similarly, adjusted EBITDA increased 14.9% to $113 million year over year. This is nearly double the revenue growth rate. Adjusted EBITDA margins increased to 23.3%, up 150 basis points year over year. Our improved operating performance enables us to increase our annual adjusted EBITDA guidance by $10 million to between $420 million and $440 million.

The midpoint of $430 million implies adjusted EBITDA growth of nearly $50 million over last year, an improvement of nearly 13%. This is more than double our revenue growth rate, illustrating the operating leverage in our model. The midpoint of our revised revenue and adjusted EBITDA guidance implies full year margins of 22.9%, 140 basis point improvement versus 2023.

When I step back, I'm particularly pleased with our focus on improving free cashflow as a conversion of our EBITDA. Year to date, we have generated $102 million in adjusted free cashflow, which is a $73 million increase versus the same period last year.

While we expect continued positive free cash flow during the second half of 2024, as you may recall, we posted outsized adjusted free cashflow during the third quarter of 2023. This was largely due to working capital enhancements and better inventory management that we continue to benefit from today. As we lap these gains in the second half of 2024, we expect a more measured outcome relative to the gains in the second quarter.

Our broad-based earning strength allows us to raise our annual guidance on adjusted free cashflow by $5 million to between $180 million to $190 million, which is based on a strong conversion of our $10 million increase in our adjusted EBITDA guidance.

Overall, I am pleased to confirm that we have fully replaced the adjusted free cashflow of last year's results, which included the benefit of both our international operations, which we subsequently divested. This validates our decision to divest those assets for $575 million in gross proceeds, focusing on the North America market to improve our efficiencies, lower our net leverage, and significantly improve our free cashflow conversion. Our balance sheet remains healthy with low net average of approximately 1.6x and more than $600 million in cash, and an undrawn revolving credit facility.

Q - Jon Kathol
Thanks, David. Robbert, can you talk about any product lines, customer segments, or geographic regions that contributed to the increased sales?

A - Robbert Rietbroek
Sure, Jon. Well, it was broad-based and balanced. We saw growth in all water channels. I think it's important to note that our overall revenue growth was over 9% when you exclude the other channel from our results.

The channel we refer to as “other” is primarily our non-core office coffee service, and some co-packing business, which has been declining as we de-emphasize and de-prioritize these businesses.

Now, our customer base actually remains very balanced with mix that is 50% residential and 50% commercial. Customer basis saw growth in the quarter. We didn't see any geographical anomalies in our growth. It really is balanced across North America.

Our dispenser business showed a quarterly decline but remains up 15% year-to-date on the volume of dispensers sold into the retailers, due to order time invariance. The dispenser sell-through is up about 4% and is a true indicator of the health of the business. We're excited about the improved consumer value of our dispensers as a result of the tariffs rolling off and prices reducing.

This should drive incremental consumers to the category, which is a good sign for the growth of future water customers. The one product and brand that continues to really stand out is Mountain Valley Spring Water, sold at retail and on-premise. Within our other water channel, it was up 87% this quarter after growing 57% last quarter. Continued success in the larger format versions of Mountain Valley also contributed to growth within our water direct channel.

It continues to attract more consumers and fulfills a super premium niche with its glass and now aluminum bottle offering. We've expanded our capacity over the last year and we're still racing to catch up with consumer and customer demand. Its natural alkalinity and crisp taste make it a huge hit with consumers. We're enabling this 150-year-old brand to reach its full potential by driving household penetration and retail and on-premise distribution.

Now, overall, I think our improved service levels are driving increased volume, retention and even sentiment scores are 94% on time in full rates or an improvement over previous periods, which drives increased revenue, improves customer satisfaction and provides a more favorable opinion of our company.

By ensuring our customers get their deliveries when expected consistently finding our products on the retailer shelves, or finding our machines working and ready to dispense water, we fulfill their demand for high quality drinking water. Specific actions taken to improve our service metrics include 6- and 7-day deliveries when necessary, filling empty shelf space and improving refill machine uptime. We're doing better, but I see room to improve even further.

Q - Jon Kathol
Thanks, Robbert. David, can you give us an update on the sale of your international businesses and any M&A activity?

A - David Hass
Absolutely. As we mentioned on our deal announcement call several weeks back, we sold the U.K., based Aimia business in June.

This was for roughly $91 million in proceeds when you include dividends pulled from the business. And last month, which happened after our close of Q2, we sold the Portugal business for approximately $19.2 million. Both divestitures added to our already strong cash position, which is now over $600 million. We remain actively marketing the remaining assets in both Israel and the Eden UK business and remain on track to divest these businesses later this year.

Q - Jon Kathol
Robbert, you mentioned last quarter that your annual revenue guidance of a 5.5% increase included 1.5% to 2% volume and the balance was price. Now you've increased your annual revenue guidance to 6%. Is the increase driven by volume or price?

A - Robbert Rietbroek
Yes, the increase in our fiscal 2024 revenue guidance is driven by incremental volume growth that we've been experiencing. Our volume growth has been strong and resilient year to date, which provides confidence in our updated revenue guidance. The revised guidance can be broken out into 3% volume growth and 3% pricing growth this year.

Q - Jon Kathol
Now let's transition the discussion to talk about the aspects of the merger with BlueTriton. Robbert, I'll start with you. It's been several weeks since the announcement. Can you provide some color on the feedback you've received from investors and further views on the announced merger with BlueTriton?

A - Robbert Rietbroek
Sure, I'm excited to talk about it. The term that keeps coming up is compelling. We're hearing that it's a natural fit and makes sense from a customer, consumer, associate, supplier and investor perspective.

It diversifies the product offering of both Primo Water and BlueTriton into more channels and categories where we can offer the consumer an incredible array of branded offerings, purified spring and super premium spring water in various pack formats.

We've received great feedback from investor calls and interactions with our research analysts. We're hearing positive reactions to the proposed combination on the merits and the potential benefits that come from the expected synergies. While we're not in a position to comment on the financial outlook of the new company at this stage, we're excited to be creating a pure play health hydration company with a portfolio of well-known brands covering the spectrum from purified to spring and value to premium. The combined company will be a steward of its water resources as a sustainability leader.

From a production and distribution footprint to our ability as a combined company to elevate the customer experience, we're excited to provide a diverse array of water solutions for the residential, the commercial, and the retail customers. You know, Jon, healthy hydration is on trend and access to high-quality drinking water sources is increasingly important. That means more demand for our products in the future. Our product offerings give consumers another choice for hydration across multiple occasions, day parts, delivery methods, and formats.

Q - Jon Kathol
David, can you bring us up to speed on the mechanics of the merger?

A - David Hass
Sure. Since announcing the deal on June 17, both teams are working on the regulatory and Primo shareholder approval processes. At Primo Water, we created a page on the investor relations section of our corporate website dedicated to the proposed merger, which contains documents, filings, presentations, and updates. And we'll continue to provide updates through that means.

We submitted our Hart-Scott-Rodino filing on July 2nd, and our Canadian filing on July 9th. We are actively working to obtain our required approvals as promptly as possible. To support that, a preliminary proxy statement has been filed with the SEC, which among other things includes information regarding BlueTriton's historical financial performance and pro forma financial information regarding the combined company.

The proxy statement is in preliminary form and subject to review and comment by the SEC Revisions to the proxy statement before it is finalized may be immaterial. We intend to hold our shareholder meeting as soon as practical once we clear SEC comments and the proxy statement is finalized. We are happy with how things have been progressing and, we'll keep you updated along the way.

Q - Jon Kathol
Robbert, can you share some insights on BlueTriton's financial performance?

A - Robbert Rietbroek
Well, the preliminary proxy statement that was filed with the SEC earlier this morning, and that is available on the investor relations section of our website, includes, amongst other things, information regarding BlueTriton's regarding BlueTriton's financial performance during the second quarter. Whether from the results in the proxy filing or when we look at the Q2 retail scan data, which shows growth in sales dollars and strong volume, we can see that BlueTriton's business performed well.

Q - Jon Kathol
Here's one for both of you. What about concerns of Primo Water getting back into retail with the merger?

A - Robbert Rietbroek
Well, let me go first, Jon, on that one. We believe the BlueTriton retail offering is a high-quality asset. We're not worried about getting back into retail with the merger.

In fact, it was an important part of the deal rationale. BlueTriton has a solid retail business, and we think it complements our Primo portfolio well. It features two $1 billion-plus brands, Poland Springs and Pure Life. And the retail scan performance of BlueTriton shows that they have performed well.

And we believe that One Rock has done a good job strengthening the retail business of BlueTriton and producing favorable trends in the business. From a sustainability standpoint, we believe both companies are leading the way in corporate accountability. BlueTriton uses a high amount of recycled content in their bottles, with targets going even higher as recycled plastic content becomes more affordable and available. Primo Water promotes the hydration and wellness benefits of drinking quality water.
Both companies are protective of their water sources and strive to be good stewards of the environment.

Q - Jon Kathol
David?

A - David Hass
Sure, Jon. The BlueTriton Ready Refresh or HOD business within their company emphasizes convenience and service in the large and fragmented category. The proposed merger will expand our reach and allow us to serve more customers with high-quality drinking water.

Overall, BlueTriton is more comparable to Primo Water's when accounting for the difference in the capitalization of bottles. BlueTriton expenses their bottles as they blow mold their large format bottles on site, whereas Primo Water buys their bottles from a third party and capitalizes the bottle purchases.

This roughly equates to a 200 basis point difference in EBITDA margins between the companies. On the retail side, the business that Primo exited in 2022 was primarily 1 and 2.5 gallon multi-serve bottles and largely a private label co-packing business.

This presented challenging financials and lacked nationwide scale, driving the business to be margin dilutive. Contrast that with BlueTriton's retail business today. Retail scan data results suggest that the retail business performs well.

Q - Jon Kathol
David, can you talk about the special dividend that Primo Water shareholders will be receiving be receiving? What about share repurchases and dividends?

A - David Hass
Absolutely. As we previously announced, we intend to issue a special dividend of up to $133 million, or $0.82 per share, following board approval and the setting of the record date and payment date prior to the closing of the proposed merger with BlueTriton. The special dividend essentially replaces the cash and then some that would have been returned to shareholders through share repurchases absent the merger with BlueTriton.

At this point, we repurchased $6.8 million in shares in the second quarter before the announcement of the proposed merger. Separately, yesterday, the Primo Water Board announced the approval of our regular quarterly dividend of $0.09 Per share.

This represents a 13% increase over last year. After the merger closing, the NewCo board expects to provide insight into long-term dividend policy.

Q - Jon Kathol
Robbert, any thoughts on the back half of 2024 and plans for 2025?

A - Robbert Rietbroek
Yes, we and BlueTriton continue to operate as two separate companies. At Primo Water, we're focused on finishing 2024 strong, and we will continue to sharpen consumer-centric approach driving volume growth.

I want to see the team continue to innovate and to create a more frictionless customer experience. Performing at a high level and executing the fundamentals will set us up for success in the balance of this year and into next as we prepare for the merger.

Q - Jon Kathol
David, same question to you. What's your focus for the back half of 2024 and into 2025?

A - David Hass

Sure. As Robbert mentioned, clearly, we want to finish 2024 strong, and the Primo Water team is focused on achieving the expected $20 million in savings in what we call the business optimization program.

This quarter, as I mentioned, we achieved additional savings in the second half of 2024 that will annualize out to another $4 million on a 2025 basis. This brings our total 2025 tracking to $8 million with continued confidence on achieving our full run rate outcome. As we head into 2025, we need to position ourselves to prepare for the proposed merger with BlueTriton subject to obtaining the required approvals.

We believe that it bodes well for customers, consumers, associates, and investors when both participants are performing well prior to the merger. As always, cash generation remains top of mind.

Q - Jon Kathol
Robbert, any closing thoughts?

A - Robbert Rietbroek
Thank you for attending today's call and for your continued interest in Primo Water. As I hope you can tell, our team is focused on enhancing our customers' experience and driving sustainable growth.

The path started is the right one to build on, and we have the tools to win. We have a lot of work ahead of us, and I, along with our team, are excited for the potential created by a BlueTriton merger. Thank you for your interest in Primo Water and joining us in the next step on our exciting water journey.

Operator
Thank you, sir. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your line. Have a lovely day.