

Mossberg's Investor Digest

Best Idea Profile:

Primo Water Corporation (NASDAQ:PRMW)

DESCRIPTION:

Primo Water Corporation provides multi-gallon purified bottled water, self-service refill water and water dispensers sold through major retailers in the United States and Canada. It is the leading water and dispenser brand, and uses three and five-gallon units. Primo claims it is better tasting than tap water, cleaner than filters, more affordable and earth friendly than single serve bottles, and less expensive than home delivery. Primo Water was founded in 2004 and has headquarters in Winston-Salem, North Carolina.

KEY INVESTMENT CONSIDERATIONS:

Industry Outlook – There is a large opportunity for growth in the U.S. and Canada given the positive trends among consumers. Although the bottled water industry took a break from its rapid acceleration through 2007, it is now steadily increasing again. There has been much more emphasis on health and wellness, particularly in the areas of obesity and sugar consumption in North America. In other words, consumers are trading in their sodas for water. Consumers are increasingly concerned about the environmental issues of single-serve water bottles, with some cities voting to phase out the use of bottled water. Their concerns also extend to municipal tap water quality, and water's taste, even that of filtered water. The bottled water industry is again approaching the \$12 billion mark and is not showing signs of slowing down.

Business Model – Primo's business model is the epitome of the recurring high-margin revenue business. It is the razor/razorblade model pioneered by Gillette in the early 1900s. It sells lower-margin dispensers in order to sell high margin water on an ongoing basis. Even the names of its three lines of business—dispensers, exchange and refill—indicate the extent to which the business is recurring. And the recurring portion of its sales, the water, offers gross margins above 30% and is about 70% of total revenues.

Strong Customer List – Primo sells to an impressive and diverse customer base: home centers, including Lowes and Ace Hardware; mass merchants, including Walmart, Target and Office Depot; grocery chains, including Kroger, HEB and Publix; membership stores, including Sam's and Costco; and drug stores. Additionally, Primo is the only single vendor retail solution available in the industry. It recently transitioned from 60 sources to a single distributor.

Strategy for Growth – Primo has 24,000 locations, with its eye on 60,000 addressable locations in the near term. It is targeting further household penetration and increased locations to drive revenues.

Executive Track Record – Primo's management was involved in Blue Rhino's successful introduction and development of the razor/razorblade model in the propane tank exchange market. Insiders own 16% of Primo stock and are incented to profitably grow the company.

Improved Financial Position – Primo recently announced a \$35 million credit facility that it believes will save more than \$2 million in interest savings annually. This can open many opportunities in its bid for expansion.

VALUATION:

With a targeted growth rate of 7 to 15% and a targeted EBITDA margin of 15% to 23%, Primo has the earnings power to produce \$25 million in EBITDA over the next three years. Revenue looking forward is fairly transparent given the recurring nature of the business. It is free cash flow positive since 2012 and has had seven consecutive quarters of positive EBITDA. Primo has the financial momentum and scale to be an attractive long-term investment.

Primo Water Corporation (NASDAQ:PRMW) Investment Data (as of 6/27/14)

Recent Price	\$4.74
52-Week Range	\$1.67 - \$4.92
Fiscal Year End	Dec
Dividend	NA
Yield	NA
Shares Outstanding	24.2 M
Average Trading Volume (3 mos)	98k
Market Capitalization	\$114.8 M
Cash	\$1.3 M
Long-term Debt	\$22.2 M
Enterprise Value (EV)	\$132.6 M
Book Value	\$1.18
TTM Revenue	\$92.4 M
P/ Revenue	1.2x
TTM EPS	\$(0.49)
P/ EPS	NA
TTM EBITDA	\$8.5 M
EV/ EBITDA	15.7x

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