Primo Water Corporation

Fourth Quarter and Fiscal Year 2021 Earnings Conference Call

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CORPORATE PARTICIPANTS

Jon Kathol
Primo Water Corporation — Vice President of Investor Relations

Tom Harrington
Primo Water Corporation — Chief Executive Officer

Jay Wells
Primo Water Corporation — Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Derek Lessard
TD Securities — Analyst

Filippo Falorni
RBC Capital Markets — Analyst

Daniel Moore
CJS Securities — Analyst

John Zamparo
CIBC — Analyst

Derek Dley
Canaccord Genuity — Analyst

Andrea Teixeira
JPMorgan — Analyst

Graham Price
Raymond James — Analyst

PRESENTATION

Operator

Welcome, everyone, to the Primo Water Corporation's Fourth Quarter and Fiscal Year 2021 Earnings Conference Call.

Thank you. I would now like to turn the conference over to Mr. Jon Kathol, Vice President of Investor Relations. Please go ahead.

Jon Kathol — Vice President of Investor Relations, Primo Water Corporation

Welcome to Primo Water Corporation's Fourth Quarter 2021 Earnings Conference Call.

All participants are currently in listen-only mode. This call will end no later than 11 o'clock a.m. Eastern Time. The call is being webcast live on Primo's website at www.primowatercorp.com and will be available for playback there for two weeks.

This conference call contains forward-looking statements, including statements concerning the Company's future financial and operational performance. These statements should be considered in connection with cautionary statements and disclaimers contained in the Safe Harbour statements in this morning's 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's full year and fourth quarter earnings announcement released earlier this morning, or on the Investor Relations section of the Company's website at www.primowatercorp.com.

I am accompanied by Tom Harrington, Primo's Chief Executive Officer, and Jay Wells, Primo's Chief Financial Officer.

As part of this conference call, we have included a deck online at www.primowatercorp.com that was designed to assist you throughout our discussion.

Tom will start today's call by providing a high-level review of the fourth quarter and our progress on Primo's strategic initiatives. Then Jay will review our segment level performance and will discuss our fourth quarter performance in greater detail and offer our outlook on the first quarter and the Full Year 2022 before handing the call back to Tom to provide a long-term view ahead of Q&A.

With that, I will now turn the call over to Tom.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thank you, Jon, and good morning, everyone.

Before I review our performance for Q4, I want to share how proud I am of the efforts of the team and pleased with everyone's continued commitment to safety and customer service as our teams have once again responded to the challenges presented by the pandemic. Our teams remained focused on inspiring healthier lives by providing water your way.

Turning to the fourth quarter, we achieved higher revenue driven by strong customer demand, particularly in our Water Direct and Exchange businesses, and implemented several pricing actions. We continue to deliver growth on Mountain Valley, America's premium spring and sparkling water brand. Our water customer base increased organically and our customer retention rates improved.

We did experience challenges like most companies, where inflationary cost pressures dominated the landscape. To address the higher costs, we implemented a series of pricing actions across our customer base. These pricing actions were insufficient to fully offset higher-than-forecasted costs for raw materials in our North American Single-Use Plastic Bottle Water business, ocean freight container rates, and tariffs incurred during the quarter. As a result, further pricing actions have been implemented in Q1 which should allow us to offset costs with pricing.

Despite the cost headwinds, we continued to invest in a customer experience, which resulted in improved service levels and higher customer retention rates. Our global customer retention rate improved by 60 basis points to 86.4 percent compared to the prior year, which compares favourably to other subscription-based companies. As Jay will outline later in his remarks, the combination of improved pricing, continued demand for our products and services, and improvement in customer retention gives us confidence in guiding to our Full Year 2022 Adjusted EBITDA of between $410 million and $420 million.

During the quarter, revenue increased 7 percent to $518 million and Adjusted EBITDA increased 5 percent to $98 million after normalizing for the fifty-third week in 2020, driven by higher demand for our products and services and improved pricing, led by our Water Direct and Exchange businesses. Water Direct and Exchange grew 7 percent, even as B2B Customer volume was softer than forecasted due to a slower B2B recovery, which we attribute to the effect of Omicron variant of COVID later in the quarter.

The Water Dispenser segment declined as a result of higher retail price points and less promotional activity driven by tariffs and the substantial increase in ocean freight experienced during the quarter. We expected to see relief from the tariffs in the fourth quarter as well as a refund. Unfortunately, that did not happen. Despite these headwinds, we sold approximately 900,000 dispensers in 2021, and are optimistic regarding the potential for tariff relief and refund of last year's tariffs at some point in 2022. Ocean freight container rates have begun to stabilize, and we believe these costs will (audio interference) over time, which we expect to support our return to growth in our Dispenser business.

Our Water Dispenser sales provide an important entry point for consumers to enter the Water category, where we can capitalize on our recurring razor-and-razorblade revenue model. The attractiveness of recurring purchase behaviour is the ability to continually generate order sales as part of our customer-for-life strategy.

As a reminder, our internal research indicates that approximately 60 percent of respondents surveyed are new to the Water category. Of those likely to become a future dispenser customer, research indicates their water purchasing preference as 45 percent for Direct, 30 percent for Exchange, and 25 percent prefer Water Refill. We should continue to capture our fair share of this growth, as a razor-and-razorblade model remains one of our strategic advantages.

Turning to operating expenses, overall profitability was adversely affected by higher operating costs during the quarter. As I mentioned earlier, the impact of higher costs outpaced our internal forecast. After averaging roughly a 4 percent increase in costs over the first three quarters of the year, we saw input costs increase more than 9 percent in the fourth quarter when compared to the prior year in the U.S. To address the higher costs, we implemented a series of pricing actions across our customer base. These pricing actions were insufficient to fully offset higher-than-forecasted costs during the quarter and further pricing actions have been implemented in Q1, which should allow us to offset costs with pricing.

As we worked our way through the fourth quarter, we started to see an increase in a number of COVID cases across our operations. Similar to the Delta variant in the third quarter, we saw hundreds of routes affected by Omicron. Fortunately, COVID case rates appear to have peaked and have dropped significantly as we move through Q1. We continue to work diligently to meet the current levels of demand, especially in our North America Water Direct and Exchange businesses.

Despite these challenges, we were able to improve our service metrics as we worked our way through the quarter. The improvement of the customer experience and a push to get closer to full staffing levels were a key focus and the result of conscious investment choices during the quarter. Although these action costs more in the short term, we believe the long-term benefits of improving the customer experience will outweigh the short-term cost supported by our continued improvement in customer retention rates.

Globally, our water customer base grew 2 percent to nearly 2.3 million customers in 2021. As I mentioned last quarter, the addressable three- and five-gallon water category of U.S. residential households alone is estimated to be between 22 million to 29 million and continues to grow. The residential opportunity for increased sales of three- and five-gallon returnable water remains a top priority, as the category has two to three times the market potential versus today's installed base, and we are focused on increasing household penetration through execution of our razor-razorblade model.

As it relates to our efforts in ESG, we remain focused on elevating our position on environmental responsibility and finding new ways to honour our commitment to protect the environment, provide quality drinking water, and manage sustainability. In December, we achieved carbon neutrality across our global operations. Major projects funded as a part of our Carbon Offset Strategy include funding water infrastructure improvements in Sub-Saharan Africa, repairing and drilling boreholes in small rural communities. By providing clean water, communities no longer need to purify water through boiling. This alleviates pressure on local forest, the predominant source of firewood, and reduces greenhouse gas emissions.

We've also funded water filtration improvements in Guatemala. Waterborne disease has been identified as a national priority in Guatemala, given the high incidence of disease and chronic malnutrition. This project distributes water filters and stoves that enable access to clean water and improve cooking conditions by increasing fuel efficiency and reducing harmful indoor air pollution. It is the first gold standard water treatment or cookstove project in the country. The project so far has benefited over 500,000 people.

In December in 2020, we became the first company to certify a spring water source under the Alliance for Water Stewardship Standards; and certified three additional spring water sources in 2021.

We will continue to transition more trucks within our fleet away from diesel powered vehicles to more environmentally friendly propane powered vehicle.

During our Q3 earnings call, and again at our Investor Day, we discussed the next phase of our transformation as a pure-play water company and leader in ESG, in that we'd begun the process of exiting the small format Single-Use Bottled Water Retail business in North America. Although it is a relatively small part of our overall business, exiting this category will make us a higher margin and more environmentally friendly business. The increasing effect of one-way single-use plastic bottles in our landfills and waterways have driven us to focus on our more environmentally friendly returnable bottle business. Our three-gallon and five-gallon bottle provides an attractive alternative to combat this challenge. Adjusting for the exit of the category, we expect revenue growth in 2022 of 9 percent to 10 percent.

In addition, during 2022, we expect to achieve our targeted $40 million to $60 million range of M&A tuck-ins, and as I mentioned earlier, our pure-play water model gives us the confidence to set a full year Adjusted EBITDA outlook between $410 million and $420 million.

I'd like to turn the call over to Jay to review our fourth quarter and full year financial results in greater detail.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Thank you, Tom, and good morning, everyone.

Starting with our fourth quarter consolidated results. Revenue increased 3 percent to $518 million compared to $505 million. Excluding the impact of foreign exchange and the fifty-third week, revenue increase by 6 percent. The gains were largely driven by growth in our Water Direct and Exchange businesses, partially offset by declines in our Water Refill and Water Dispenser businesses.

Adjusted EBITDA was flat to last year at $98 million. Excluding the effect of the fifty-third week in the prior year, Adjusted EBITDA was up 5 percent in the quarter. As Tom discussed, the effect of higher cost, coupled with softer B2B volume, drove lower than expected profitability. The later stages of the quarter, we saw the effects of the Omicron variant, which caused B2B volume to come in lower than expected.

The higher COVID rates also affected our route drivers and caused us to increase spending to deliver our goods and services to customers. These costs along with a push to get to full staffing levels were partially offset by increased pricing taken during the fourth quarter. The major buckets of higher costs include material cost associated with our North America Single-Use Water Retail business, ocean, freight, and labour. As Tom mentioned, we had forecasted and priced for higher costs; however, these costs came in considerably higher than expected. The additional pricing taken in the fourth quarter, and again in the first quarter, should allow us to now offset these increased costs.

Turning to our segment level performance for the quarter. North America revenue increased 1 percent to $387 million compared to $385 million. Excluding the impact of foreign exchange and the fifty-third week, revenue increased by 6 percent, driven by growth in our Water Direct and Exchange businesses, partially offset by a lower revenue from our Water Refill and Water Dispenser businesses.

Adjusted EBITDA in North America increased 4 percent to $85 million. Excluding the impact of the fifty-third week, Adjusted EBITDA was up 10 percent in the quarter.

Turning to our Rest of World segment, revenue increased by 9 percent to $131 million. Excluding the impact of foreign exchange and the fifty-third week, revenue increased by 9 percent. The increase was driven by growth in residential customers, with revenue from residential customers being up 15 percent. Revenue from B2B customers up 5 percent for the quarter, as the performance of our Water Direct B2B customer base remains tied to the relative level of the return to (audio interference) each of the countries we serve. We continue to work toward an efficient and low-cost rollout of our products and services for residential customers in Europe to further diversify our customer base and better balance the customer mix.

Adjusted EBITDA in the Rest of World segment decreased 9 percent to $20 million, as government subsidized furlough programs are ending in many European markets and we're investing in sales and marketing to drive volume and revenue growth.

Turning to our liquidity position and balance sheet. We end the quarter with a cash balance of $128 million and available net borrowing capacity on our cash flow revolver of $80 million for a combined total liquidity position of $208 million. Our net leverage ratio is 3.8 times, and as a reminder, we are now targeting a net leverage ratio of less than 2.5 times by 2024.

Looking to the first quarter, based on the information we have available to us as of today, we currently expect consolidated revenue from continuing operations to be between $510 million and $530 million. We also expect that our first quarter Adjusted EBITDA will be in the range of $80 million to $90 million. For the Full Year 2022, organic revenue growth is projected to be 7 percent to 8 percent and overall revenue growth is projected to be 9 percent to 10 percent, adjusted for the exit of the North America Single-Use Retail Water business and including the revenue from the tuck-in acquisitions made during 2021.

As Tom mentioned, the exit of the North America Single-Use Retail Water business is moving quickly, and 2021 these products accounted for revenue of approximately $142 million. We now expect that 2022 revenue for this product line to be about $40 million with minimal effect on Adjusted EBITDA. We still expect to be out of this category by mid-year.

We are forecasting our annual Adjusted EBITDA to be between $410 million and $420 million. We also expect around $10 million of cash taxes, $60 million of interest, as well as capital expenditures of approximately $200 million. The capital expenditure figures include incremental spending, as we discussed during our recent Investor Day, which is being used to support our growth outlook and EBITDA margin expansion. The multiyear incremental spending will begin in 2022 and will show returns in subsequent years.

Key initiatives to be funded from the incremental CAPEX include driving digital growth, leading dispenser innovation, building a more environmentally friendly delivery and service fleet, installing more efficient water production lines, which will reduce water usage and increase productivity, and driving growth and refill with Sipple on-the-go units and new filtration innovations like BIBO.

Earlier this week, our Board of Directors authorized a quarterly dividend of $0.07 per common share. This dividend represents a 17 percent increase over previous quarterly dividends. As discussed during our November investor day, our growth outlook and increased free cash flow generation can fund our growth and an increase in our annual dividends. Our path to a multiyear dividend step-up includes an increase in our quarterly dividend per share by $0.01 in 2022, another in 2023, and another in 2024.

Other aspects of capital deployment include continuing our tuck-in M&A. During the fourth quarter we announced the acquisition of Clear Mountain Refreshment Services in Little Rock, Arkansas; Water Event, which operates five locations in the Dallas-Fort Worth metroplex; and the purchase of SipWell in Belgium. The addition of SipWell makes Primo the leading provider of sustainable drinking water solutions in Belgium, expanding the Primo footprint and furthering our vision of providing sustainable water solutions whenever, wherever, and however our customers want them.

For 2022, we are again targeting $40 million to $60 million of tuck-ins and remain focused on executing the robust pipeline of tuck-in opportunities in front of us. Our long-term organic growth outlook has not changed. In terms of our outlook for 2024, we are forecasting high single-digit organic revenue growth, targeted annualized Adjusted EBITDA approaching $525 million, Adjusted EBITDA margins of 21 percent to 22 percent, adjusted earnings per share of $1.10 to $1.20 per share, net leverage of less than 2.5 times, and return on invested capital greater than 12 percent.

I will now turn the call back to Tom.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Jay.

Looking ahead, we remain focused on executing our differentiated water-your-way platform, and we will leverage our pure-play water model to drive revenue growth of 9 percent to 10 percent in 2022, adjusting for the exit of the North America Single-Use Plastic Retail Water business and including the revenue from the tuck-in acquisitions made during 2021. We will continue to enhance the customer experience by building out more diverse e-commerce solutions and improving the customer experience through flawless delivery execution.

We have two important global initiatives that we believe will make a difference in customer experience and revenue. The new refreshed North America mobile app will be launching in the second quarter with an easier experience for our customers and, most importantly, with new features that provide easy access for support with more channels such as live chat. The second initiative is the launch of a global direct-to-consumer web shop later this year that will accelerate our dispenser sales and introduce an on-demand approach for all things water. By taking a global approach in the launch of these two digital platforms, we see efficiencies in developmental costs, accelerated learning, and further enhancing our Primo-branded global platform. We will continue to execute our razor-razorblade model with growth in the number of dispensaries sold, driving top line growth through the sale of water products.

Earlier this month, we announced the launch of a new alkaline water brand, Primo Plus. Primo Plus alkaline water will complement our existing portfolio, as alkaline water is a growing trend globally. Primo Plus alkaline water has a pH level of 9.5 at the time of bottling and is an ideal hydration solution sold in three-gallon bottles. It is currently available for Water Direct customers in limited U.S. geographies and will be expanding to select grocery and retail locations through our Water Exchange program during 2022.

Supporting our growth are more structural and dramatic tailwinds that are driving consumers toward healthy hydration solutions. The growth in the Health and Wellness category continues to support our prospects of gaining share of the broader beverage category. COVID and its variants continue to elevate the health and wellness conversation, and consumers are increasingly conscious of their overall health and wellbeing. In addition, the perception of the declining quality of municipal tap water is well documented, which supports the growth of our products and services. Tap water as the primary drinking source is expected to continue to decline in all parts of the world for the foreseeable future.

As Jay noted, we expect our consolidated first quarter revenue to be between $510 million and $530 million and for our Adjusted EBITDA to be between $80 million and $90 million. For Full Year 2022, we're forecasting revenue growth of 9 percent to 10 percent, adjusting for the exit of the North America Single-Use Retail Water business and including the revenue from the tuck-in acquisitions made during 2021, and are forecasting our Adjusted EBITDA to be between $410 million and $420 million.

We continue to see the elevated demand in the residential sector as the return-to-work aspect of the B2B sector has once again been delayed with the emergence of the Omicron variant of COVID. Fortunately, COVID case rates appear to have peaked and have dropped significantly as we move through Q1. We're also maintaining a strong pipeline of M&A targets, which we expect to execute during the remainder of the year.

Once again, I'd like to thank the Primo water associates across the business for their tireless efforts to serve our customers.

With that, I'll turn the call back over to Jon to move us to Q&A.

Jon Kathol — Vice President of Investor Relations, Primo Water Corporation

Thanks, Tom.

During the Q&A, to ensure we can hear from as many of you as possible, we would ask for a limit of one question and one follow-up per person.

Thank you. Operator, please open the line for questions.

Q & A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session.

Your first question comes from Derek Lessard with TD securities. Please go ahead.

Derek Lessard — Analyst, TD Securities

Yes. Good morning, gentlemen, and hope you're all well.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Good morning, Derek. How are you?

Derek Lessard — Analyst, TD Securities

I'm very good. Thanks.

You guys held your Investor Day last November, which in these times feels like a really long time ago now. But if I go back to that period, you sounded really confident, almost excited, in the outlook. I guess my question really is, do you think that these results in any way temper or impact that longer 2024 outlook that you have?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, Derek. This is Tom.

The short answer is no. If you look over the last two quarters, the Delta variant and the Omicron variant have provided us with unexpected short-term headwinds. The Company, we, decided to continue to invest in service, because we think that's in long-term best interest of everyone, our customers, and our stakeholders. So, we chose to keep that investment and try and service through these (inaudible) anomalies, I hope, so they have not been our friend.

I'm actually more bullish today than I was back in Investor Day. We still have positive tailwinds consumers are going to look for our brands, they're going to look for our products, they're going to look for our services more in the future than they have in the past, so we think that's a positive place for the Company to be. We continue to grow our market share. We continue to grow profitability. I'm confident, and over the last few years, as you know Derek, this is the first time I've said 9 percent to 10 percent growth. So, we've become a growth company, and we're confident in our ability to achieve those numbers.

We also continue to make appropriate investments. We're investing in assets to improve efficiency and effectiveness. We continue to invest in CX. We'll continue to make investments in ESG, which we believe matters and will become a tailwind for us. And we have the capital structure to continue to accelerate growth and execute against our tuck-ins.

As I said, I'm more confident about what our outlook is for '24 than I was when we did this in November. Omicron has not been my friend. Neither was Delta. But that's now in your rearview mirror, I hope.

Derek Lessard — Analyst, TD Securities

Okay. Just maybe one follow-up for me, and that’s very helpful. Thanks.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Derek.

Derek Lessard — Analyst, TD Securities

As it relates to everything that you do consider transitory, so Omicron, inflation and supply chain, just wondering how these pressures have been trending almost now that we're two thirds the way through Q1?

I'll pass it to Jay, but our forecasting assumes status quo. We didn't anticipate Omicron in Q4, it created challenges, as we've articulated, to us from the labour perspective servicing our customers. It also had a negative impact on the B2B commercial volume recovery that, frankly, we didn't anticipate that we'd get another spike.

Jay, anything to add?

Jay Wells — Chief Financial Officer, Primo Water Corporation

The other thing that Tom didn't mention was within the forecast and guidance that we provided, it was the end of tariffs on our water dispensers that we're importing from China. If you look at last year, we spent about $13 million in tariffs. Now, keep in mind, $8 million was in CAPEX, those are the coolers that we buy to lease to our customers, and about $5 million was in COGS, those are our resell coolers. Within my forecast was getting that refunded; that's on me, that's part of a miss. I assure you, it's not in my current guidance either, because the government has moved slow. We're still optimistic we're going to get it back, so I view that now as upside on my forecast and guidance versus the risk I had when I expected it last quarter. That's once on me, shame on me-type forecasting, let's put it that way. The same with recovery. We were trending really good on recovery from COVID. We thought that trend would continue, and it didn’t; it actually reversed a bit in Q4.

Those are the two of the main things that were assumptions in my forecasts that weren't accurate. Again, I'm not going to forecast a significant recovery throughout this year. I'll take it as it comes, but I would view that more as opportunity than risk if it doesn't come.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

And then the key points on the tariffs: if we get it, terrific. But we're not creating a hurdle for ourselves here.

Derek Lessard — Analyst, TD Securities

Okay. (Multiple speakers) Okay, thanks for all that.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Derek.

Operator

Your next question comes from Nik Modi with RBC Capital Markets. Please go ahead.

Filippo Falorni — Analyst, RBC Capital Markets

Hi. Good morning. This is Filippo Falorni on for Nik. How are you guys?

Jay Wells — Chief Financial Officer, Primo Water Corporation

Good.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Very good. Good morning.

Filippo Falorni — Analyst, RBC Capital Markets

Good morning.

First, on the cost front, can you remind us after the exit of the North America Single-Use business how much of your cost is in commodities? And what are the biggest commodity exposure for your business? And then, more broadly, in terms of cost inflation, I guess, what are you assuming for 2022 in terms of ELB or cost inflation?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes. I'll take a piece of that. This is Tom, and then give it to Jay.

On our Retail Bottled Water business, the commodity issue was resin for the high-density polyethylene bottles. Also impacted us on corrugated, the box, shrink wrap, you name it. All of the components of that business, which I'm happily on schedule to exit in the next two months, were negatively impacted by cost inflation.

Jay, do you have some numbers that…

Jay Wells — Chief Financial Officer, Primo Water Corporation

Yes, no, I mean, you really look at year over year, our main cost buckets that we said were up 9 percent versus the trend to 4 percent to 5 percent. I'd say almost half the bucket were the first items that Tom mentioned, and it was material cost (audio interference) thankfully, the Single-Use Plastic Retail business that we're exiting, so that's one of the many reasons we are getting out of that business.

I would say when you look at the other half, it was really two tranches. It was ocean freight and tariffs, and then it was labour. We are going to see having to give our folks higher raises. Also please keep in mind our RSRs, especially in North America, are predominantly commission based. As we take price, we are going to pay more in commissions. We get the majority of it, be sure, but we will see labour.

I would say assuming we are, and we will be by mid-year, fully out of the Retail business discussed, that will take the main material cost-type inflation. Tom and I already talked about tariffs. We are seeing ocean freight start to moderate and improve a bit as we go into this year, so that's the other cost I look at. And then the last is really labour. We're a delivery company. We have our RSRs delivering, providing our customers good service, and we want to make sure we provide our customers the best service we can, so retaining and developing those associates is key as part of our associate experience that we focus on.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

While we anticipated inflation rolling into Q4, we didn't anticipate, frankly, it would be 2x. And we had taking pricing across the customer base based on what we saw when we were in Q3, and executed that in the end of August. We've taken another action that has been implemented during January based on the realities of what we saw in Q4. We got we got the 2x, and then we've taken the action to address it on go forward.

Filippo Falorni — Analyst, RBC Capital Markets

Got it. That makes sense. That's very helpful. Then I guess, price, you commented a bit on taking another action. Would you feel like you're in a good position now? Would you consider incremental actions as the commodity or the cost environment were to (inaudible)?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, so we think we've covered as we sit here today. As you can imagine, we're like many other companies watching costs like a hawk. And if we're required to act, we will. The good news is our customer retention rates continue to improve, which is partially because of our decision to not cut those costs and focus on the customer experience, which is ultimately the key driver of our success, our 9 percent to 10 percent growth, and our ability and confidence in the multi-year 2024 outlook.

Filippo Falorni — Analyst, RBC Capital Markets

Great. That's very helpful, guys. Appreciate it.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thank you.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Thank you.

Operator

Your next question comes from Daniel Moore with CJS securities. Please go ahead.

Daniel Moore — Analyst, CJS Securities

Thank you, Tom. Thank you, Jay.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Hi, Dan. How are you?

Daniel Moore — Analyst, CJS Securities

I'm good. I'm good.

Maybe focus on the go forward. Great colour, by the way, in terms of the impact of the tariffs; that helps clarify things quite a bit. In terms of the growth expectation, 8 percent to 9 percent organic, how much of that is volume, and how much of that is price, roughly, given all the price you've had to and been able to take?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, just a point of clarity, and then I'll pass it over to Jay.

Organic, I believe it's 7 percent to 8 percent, and then if you factor…

Daniel Moore — Analyst, CJS Securities

Yes. My apologies. Yes.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, no worries. Just so we're clear, the 9 percent to 10 percent has the exit of that…

Daniel Moore — Analyst, CJS Securities

Overall. Yes.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, retail jazz, and then the benefits of some tuck-ins. Just to be clear.

Jay, some colour?

Jay Wells — Chief Financial Officer, Primo Water Corporation

We've talked about it before, and Tom mentioned it on the call, that our water customer base is up 2 percent. That is driving the growth, and a key focus is continue on the customer experience, improved ads, reduced our quit rate, so customers are generating a very good part of that. I would say when you look on the volume side, on top of that, I think you heard a little bit of a tone. I think we've moved a little bit on a conservative side on the B2B side to more run current trends. But we're continuing to fit within our forecast to be very bullish on the residential side. The residential side should continue to derive about another 1-plus percent on volume. Commercial gives give us an upside if we don't have another variant of COVID, and then pricing would be the remainder of it, Dan.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

The other piece I'd add is, last year, ’21, we sold approximately 900,000 dispensers. They create what we call water-only customers, which is a terrific customer, largely residential. As the ocean freights have begun to I won't say normalize but ease, and hopefully we have a resolution on the tariffs, we expect to accelerate that Dispenser business, which will give us growth in that customer base that buys three- and five-gallon containers from us.

That’s part of the growth story. People love our brands, and we’re just finding different ways to give them water their way.

Daniel Moore — Analyst, CJS Securities

Helpful, and clearly impressive customer retention in the face of those multiple price increases. The growth in terms of Rest of World versus North America, you just gave us some inkling. But do you expect to continue to drive retail penetration in Rest of World, and what are the kind of relative growth rates embedded in the guide? Thanks again.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, I think that we were quite pleased in 2021 with our residential performance in the Rest of World. Unfortunately, if Delta and Omicron spiked in North America, there were more than two spikes depending on the country you're in in Europe. But we think that the markets are accelerating their return, if you will, and easing mass guidance, offset by whatever happens in the Ukraine.

We think we're in a good spot. We're confident about our ability to grow the Residential business. We will develop the solution that we call Sipple on-the-go, which we think is a real solution to grow our revenue and volume in the continent, and we'll go there first later in 2022.

Jay Wells — Chief Financial Officer, Primo Water Corporation

I'm very excited on the quarter, 15 percent residential growth, 5 percent B2B growth. I mean, that is great that, as we've talked before, Europe has been a flattish to declining business. So, through all of the efforts we're making, we've turned the top line into growth. Now, we did have some bottom-line pressures, and we will as we lap the furlough programs, as we get the employees back in, and then and only then can you right size the organization, because you cannot right size organizations while individuals are on furlough programs, so be assured that we'll adjust our cost base to the right level.

But the exciting part is that type of top-line growth out of Europe is something we did not see when we diligenced even many years ago, and we haven't seen since we bought them. I think Europe's in a very good space going forward.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

It’s become a tailwind.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Yes.

Daniel Moore — Analyst, CJS Securities

All right. And the tariffs, if you did get them back, would be up to a $13 million potential benefit, or is that the right way to think about it? (Multiple speakers).

Jay Wells — Chief Financial Officer, Primo Water Corporation

Remember, $8 million was CAPEX, so if we get that back, that's not an EBITDA benefit. But $5 million did go through COGS as a cost of goods sold of the dispensers that we sell in retail. That would be a benefit flowing through.

Daniel Moore — Analyst, CJS Securities

Very helpful. Thank you.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Dan. Appreciate it.

Operator

Your next question comes from John Zamparo with CIBC. Please go ahead.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Good morning, John.

John Zamparo — Analyst, CIBC

Good morning, guys.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Hello, John. Good morning.

John Zamparo — Analyst, CIBC

Good morning.

I wanted to follow up on revenue in the quarter, and appreciate the commentary so far. You mentioned some headwinds from Omicron, of course. But can you add some colour, particularly on the Refill and Filtration segment and the other segments? Seems like you saw some softness in those. I wonder if that was impacted by Omicron, or the furlough programs you're talking about. I know there's a customer loss in the Refill side. But any commentary you can add on those two segments would be helpful.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes. I think on Refill there's a couple of things that were a headwind in the quarter, and there is a direct correlation to Omicron and/or the Delta variant, frankly, at the end of Q3, and it has to get to retail store traffic. So, if foot traffic is down retail, then the number of customers that pass our outdoor refill machine will be lower, and the number of customers that go through the aisle for the indoor machine is lower. So naturally, we're going to be negatively impacted from a revenue perspective.

We're cautiously optimistic, but we're not baking in any—we're taking the appropriate approach that says we're going to take steady state in terms of those businesses, as opposed to expecting that it gets better because. Which was a bit of our problem in Q4 thinking that Delta was good, things look great, and then Omicron hit us again.

Filtration was also going to be related to Omicron, if you think about traffic and how many commercial opportunities don't exist today partially because of work from home. As that business segment is still either in decline, or not yet stable because of the variant, our ability to attract new customers is negatively impacted in short term, which has a direct impact on the top line.

Jay Wells — Chief Financial Officer, Primo Water Corporation

I think you mentioned Other Water also, John, you're going to see that decline in North America. That's the exit of our Single-Use Plastic Water business, so that is what that decline that you see in the Other Water.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

And that declined faster than we anticipated post our announcement, which gets us out of the business.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Yes. That business, as I mentioned, was $142 million last year. It's going to be $40 million this year, about $20 million each quarter. On revenue, since we're on it, we posted a supplemental deck on our website, and if you look at Slide 23, that will give you a good view of our quarterly revenue last year, then it minuses out the revenue associated with this Single-Use Plastic Water business that we're exiting, and then it's really 9 percent to 10 percent growth on that number each quarter, and then I'd add another $20 million in Q1 and $20 million in Q2 (audio interference) add back the little bit of revenue we will still have in that channel for the front half of this year. So, that's how we look at it. But it really is the exit of the Retail business we've discussed.

John Zamparo — Analyst, CIBC

Okay, that's very helpful. Thank you for that.

My follow-up is on the CAPEX guidance of $200 million, just thinking about the Investor Day, or maybe it was Q3, but I think you'd said 7 percent of sales as a rough guide and then $50 million of additional projects to be spread over the next three years. If you do that math, you get a bit below the 200. I'm wondering, have you front-loaded some of those projects, does the 200 now reflect paying the tariffs or the CAPEX portion of it? Any other colour there you can add would be helpful.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

I'll give you kind of the way I think about the phasing, is that we will make investments in 2022, both on efficiency projects, as well as growth projects, but we won't see that benefit until later on. If you think about, frankly, ’23 and ’24, you have to execute those projects and do work and plants and build a simple machine that works globally. We'll make those investments this year, we'll see future benefit in ’23 and ’24.

The CAPEX, Jay, I’ll flip to you on.

Jay Wells — Chief Financial Officer, Primo Water Corporation

I think the difference you're trying to work to is probably the tariffs that I referred to. If it goes way up, we would get closer to the number your referring—not the refund, but just the pure in your CAPEX (inaudible). That's probably the difference. That's above and beyond the 7 percent of revenue. But when that goes away, we'll get back to about 7 percent, so I would say that the tariffs on the dispensers that we rent to our customers, that CAPEX is really probably the difference that you're looking for.

John Zamparo — Analyst, CIBC

Okay. Understood. Thank you very much.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, John. Appreciate it.

Operator

Your next question comes from Derek Dley with Canaccord. Please go ahead.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Good morning, Derek.

Derek Dley — Analyst, Canaccord Genuity

Hi. Good morning.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Hello, Derek.

Derek Dley — Analyst, Canaccord Genuity

Just on the price increase that you expect. Jay, did I hear you correct, it's going to be about 5 percent to 6 percent for 2022?

Jay Wells — Chief Financial Officer, Primo Water Corporation

I think you're roughly correct. If you think and you look at inflationary numbers right now and you ignore what happened in Q4, that's not far off of inflation, and that's what we're pricing to cover the cost of increase plus a little bit more, so you've got it about right, Derek.

Derek Dley — Analyst, Canaccord Genuity

Okay, and how does it compare to the price increase that you took in Q4?

Jay Wells — Chief Financial Officer, Primo Water Corporation

Well, it's kind of more of a combined that I'm doing the rollover benefit on the full year and what we've taken. And just point of information, we have taken it, it's gone through, it's gone to our customers, so it's in place, we pocketed that. And keep in mind, we're still going to do our regular pricing on top of that too. This was more just acceleration of certain others. So, it's a combination of rollover benefits, the pricing that we took, right at the end of January, beginning of February, and then our normal pricing that we take throughout the year gets you to that number, Derek.

Derek Dley — Analyst, Canaccord Genuity

Okay. No, got it. That's helpful. Then maybe, Tom, just your comment on freight. Can you quantify that a little bit for us? I get it, it’s still elevated, but normalizing. But how does that compare to what you've seen over the last two quarters?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, I'll give you a couple of numbers to put it in context.

I paid as high as $25,000 a container, and pre all of this, it would be something close to $5,000 if you went back to before the spike, so that's the order of magnitude of the change. We paid down under $20,000 or less now, so it's beginning to work its way closer to $15,000 than $25,000. We haven't built all that benefit in, because we need it to be more than 10 containers of trend, right. Jay said it before, you can accuse me of being conservative. I'm just being thoughtful. I don't want to make a tariff mistake again, and I'm complicit with Jay on that. We want to make sure that it's trendable and bankable, so that's really how we think about it.

Now, you may also ask it's still, if you're in Long Beach, I think the last numbers I looked at was 80 days. But we built that into our demand plan, so we think we have the appropriate flow of assets. So, it doesn't impact our ability to acquire customers; but the pricing offsets it, and we've baked in now that 80 days into that demand planning model, which, frankly, last year was a catchup, right. You went from whatever it was, less than 30 to 80, practically overnight. All that now we kind of modelled into our go forward operating plan.

Derek Dley — Analyst, Canaccord Genuity

Okay, that's great. And then can you just maybe talk about the business that's coming through your website and your E-Commerce business? How has that been growing over the last year? Can you provide what percentage of revenue it represents?

Tom Harrington — Chief Executive Officer, Primo Water Corporation

I can do some of that. Let's go with Europe. You remember we stood up websites if you go back in May of 2020. We now have websites up in all markets in the Rest of World, and it led to something on the order of 25,000-plus net new customers on the residential side in Europe, which was a positive tailwind for us as we dealt with the high percentage of our customer base in Europe that was Commercial business, so that has worked quite nicely.

Our residential mix is higher in North America. We are generating more customers from digital. We're rolling out a new app in North America, early Q2, which we expect to help us drive customers. And we are building in process of global call it e-commerce web shops, Derek, that will enable us to accelerate Dispenser sales and Water sales through this platform as we go forward. We haven't stood them up everywhere. We're still in the learning stages, but we are selling dispensers, and we actually sell water on those sites. So, we think it'd be a good component of that, ultimately, 9 percent to 10 percent growth model.

Derek Dley — Analyst, Canaccord Genuity

Okay, great. Thank you very much.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Derek.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Thanks, Derek.

Operator

Your next question comes from Andrea Teixeira with JPMorgan. Please go ahead.

Andrea Teixeira — Analyst, JPMorgan

Thank you. I wanted to just follow up on the organic growth guidance and on the commentary about the 1 percent volume guide for residential embedded into total top-line growth. I'm a bit surprised; maybe I’m understanding it the wrong way. You had it 900,000 new dispensers sold last year. I'm not sure if it's more exchange-related, and within the razor-razorblade model that those jugs that go into there will be accounted for in the residential customers. And so, in other words, are you being just conservative because of the tough comparisons for residential, or you're assuming that reopening, the commentary about commercial customers, that you'll be more conservative on those and/or the frequency of purchases?

And related to that, what we saw in the fourth quarter as we enter the first quarter, did the Omicron impact subside during the beginning of the year? Was there any major customer that you lost during those logistics issues? And perhaps comment also on the churn rate after you took pricing.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Okay, Andrea. Good morning.

Andrea Teixeira — Analyst, JPMorgan

Good morning.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

I may take these backwards.

Customer churn and our retention in Q4 was 60 basis points better, 86.4 percent. And our 2021 pricing was initiated, implemented, let's call it September 1. That number did not spike. It's part of our investment with the route associates in terms of servicing the customer investments and our call centre to make sure that we gave continued service despite the Delta and Omicron variants. So, that's a pretty good indicator for us that we are getting the price we need and we've seen it flow through and we haven't chased off customers. We're not seeing any material change early in Q1.

In terms of where we are with the Omicron, it's like other things I've read, is the number of cases has dropped off markedly. But, in October and at the end of the quarter we had some discussions. I was really probably too bullish about how that turned out, and Delta became Omicron. So, yes, I would be conservative about that. We're expecting steady state; no meaningful positives from that benefit of, let's hope, another variant.

On the dispensers, the way to think about it is we get customer acquisitions in Water Direct from people who rent coolers from us. You can relate that to Jay's comments about the $8 million in CAPEX. And then we separately sell 900,000 coolers through a number of large retailers and through e-commerce. In our script, we talk about roughly 45 percent of the customers who bought—roughly 60 percent of the customers that buy dispensers are new to the category, I think it's the number. We can validate that. Forty-five percent of them prefer Water Direct, 25 percent prefer Exchange, and 30 percent prefer Refill. And we get our fair share of that in terms of our market share, so we would expect those water dispenser purchases to come into our family of products, brands, and products either in Direct, in Exchange, or in Refill. That was really around the water only that I talked about, and that's how we categorize them, and they would be part of our growth story, largely residential.

I think I got it.

Jay Wells — Chief Financial Officer, Primo Water Corporation

You got it.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

I think I got all three, Andrea, but I'm not sure. Hopefully that helps.

Andrea Teixeira — Analyst, JPMorgan

This is super helpful. Yes. No, absolutely. But just double-clicking on that, the 1 percent that you’re assuming for residential in 2022. How did that number compare? How much did you grow in volume for residential customers in 2021 and in 2020, if you can give us that kind of progression of household penetration and growth?

Jay Wells — Chief Financial Officer, Primo Water Corporation

I don't have that number at hand. My apologies. But let me just kind of repeat what I said earlier; it might have been missed a little bit. We mentioned that our customer base within Water is up 2 percent. We're bringing that tailwind in. Tom talked about our retention rates improving, our focus on the customer experience, bringing that. That will give us that organic growth.

Then what we see in volume growth is another 1-plus percent, maybe getting up to 2 percent. And that's really being led by residential, and that's pretty typical, pretty standard. Let's ignore the unusual fluctuations during a pandemic, but that's normal. What we're not factoring in is much more recovery on the commercial side, not to say that it's not going to be there, but I'm just not going to include it in my forecast, because I'm not going to forecast COVID recovery anymore. And then the remaining is really the price increases that we're taking.

Andrea Teixeira — Analyst, JPMorgan

That's perfect. Thank you so much for reiterating that. Appreciate it. Pass it on.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Thank you.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thanks, Andrea.

Operator

Your next question comes from Graham Price with Raymond James. Please go ahead.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Good morning.

Graham Price — Analyst, Raymond James

Hi. Good morning.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Good morning.

Graham Price — Analyst, Raymond James

Thanks for (inaudible).

You previously gave the colour around the revenue outlook for the single-use divestiture asset. Just wanted to double check that $40 million, does that assume that the asset would be divested maybe some time next quarter? Was also wondering on the impact of that divestiture on margins and profitability in your 2022 outlook.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Yes, it's our expectation that we will be completely out of this business by the end of Q2, and then Jay referenced the numbers that it was $142 million in prior year. We expect roughly $40 million this year, which is an update since Investor Day, because it was begun to exit a little bit quicker than we originally expected.

And then on the margin, Jay will you give some insight on it?

Jay Wells — Chief Financial Officer, Primo Water Corporation

Again, specifically for these types of questions, I did add a slide to our supplemental deck. It's in the Appendix, Slide 23, and it does show our revenue by quarter last year minusing out the benefit of this specific, so you can see it runs about somewhere in the $30 millions every quarter to get to the $142 million. Then how I'm modelling it in my projections, what we've got left, kind of feeling like we have—kind of what I'm doing with the depreciation on these assets. If you see a little spike in depreciation, I'm kind of straight lining the $40 million out until the end of Q2. So, $20 million this current quarter, $20 million next, on top of the growth we'd get off of the net numbers shown on Slide 23.

Does that make sense?

Graham Price — Analyst, Raymond James

That does. That does. Thank you for that. Just a quick housekeeping follow-up. I saw a spike in D&A expense for 4Q.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Yes. I just tried to answer that question as part of the (inaudible), because I knew you probably would have that question too. Yes, what you're really seeing, once we decided to get out of the business by the end of Q2, every asset within this business under the GAAP accounting rules, you accelerate the depreciation and you depreciate (inaudible), amortize it over the remaining term. So, you're seeing the accelerated D&A associated with the business that we're exiting.

Graham Price — Analyst, Raymond James

Okay. Sure. Understood. Thank you.

Jay Wells — Chief Financial Officer, Primo Water Corporation

Thank you.

Tom Harrington — Chief Executive Officer, Primo Water Corporation

Thank you very much.

Operator

There are no further questions at this time. Please proceed.

Jon Kathol — Vice President of Investor Relations, Primo Water Corporation

This concludes Primo's fourth quarter results call. Thank you all for attending.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a great day.