

Cott Corporation

Fourth Quarter and Fiscal Year 2018 Earnings Release

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PRESENTATION

Operator

Good morning, and welcome to the Cott Corporation Fourth Quarter and Fiscal Year 2018 Earnings Release.

I will now introduce the Vice President of Investor Relations for Cott Corporation, Mr. Jarrod Langhans. Please go ahead.

Jarrold Langhans — Vice President, Investor Relations, Cott Corporation

Welcome to Cott Corporation's fourth quarter and fiscal year 2018 earnings conference call. All participants are currently in listen-only mode.

This call will end no later than 11:00 a.m. Eastern Time. The call is being webcast live on Cott's website at www.cott.com, and will be available for a playback there until March 8, 2019.

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 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 US and Canadian 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, is available in the Company's fourth quarter and fiscal year 2018 earnings announcement released earlier this morning, or on the Investor Relations section of the Company's website at www.cott.com.

Today, I'm accompanied by Tom Harrington, our Chief Executive Officer, and Jay Wells, our Chief Financial Officer. As a part of this conference call, we have included a deck online at www.cott.com that was designed to assist you throughout our discussion.

With that said, Tom will start this morning's call with some thoughts on our Company overall before turning the call over to Jay for a discussion of our fourth quarter and full year consolidated financial performance, the results of both our Route Based Services segment and our Coffee, Tea and Extract Solutions segment, as well as our 2019 expectations, before handing the call back to Tom to comment, before moving to Q&A.

With that, let me now turn the call over to Tom.

Tom Harrington — Chief Executive Officer, Cott Corporation

Thank you, Jarrod, and good morning, everyone. In looking at 2018, I'm pleased to report that our results continue to come in as expected, our strategy is working, and we're well-positioned for the future.

2018 was a very busy year for us from a transactional and capital deployment viewpoint. We divested our traditional business, which allowed us to reduce our outstanding debt by approximately \$1 billion, and in turn created a business services company focused on growing better-for-you categories.

We more than doubled up on our tuck-in acquisition efforts, which not only drove customer density across our footprint, but also filled the distribution void in the northeast with the Crystal Rock acquisition, and added an American premium brand in Mountain Valley to our portfolio. Both of these transactions have gone well and are tracking at or ahead of our integration plans, and we believe, are great additions to our business. And we returned over \$100 million to our shareholders through a combination of share buybacks and dividends.

As I look back on 2018, I am proud of what our associates were able to accomplish, even when challenged with a variety of market pressures, such as increased freight and transportation costs. Overall, we generated good top line and free cash flow growth, with revenue coming in on track at plus 5 percent, with strong growth in free cash flow which came in above our projection, even when backing out the working capital benefits and EBITDA, coming in within the range that we forecasted on our last call, while at the same time allowing us to accrue additional short-term incentives for our North American Route Based Services business, rewarding them for a job well done.

As we look to 2019, we're positioned to benefit from the continuing growth in both the Water and Coffee categories, with our Route Based Services operating segment leading the charge. We are confident in our ability to meet our expectation of 4 to 5 percent top-line growth, which, as shown on Page 6 of the deck that Jarrod referenced, we have achieved over the last three years. We are equally confident in our ability to deliver on our forecast of 150 million-plus of free cash flow.

I will now turn the call over to Jay, who will review more specifics on our performance. Jay?

Jay Wells — Chief Financial Officer, Cott Corporation

Thank you, Tom, and good morning, everyone. Starting with the quarter, good top-line performance across our Route Based Services segment drove a consolidated revenue increase of 5 percent; 7 percent, excluding the impact of foreign exchange, and adjusting for the change in average cost of coffee within our Coffee, Tea and Extract Solutions segment.

Operating income increased by \$4 million and adjusted EBITDA grew to \$72 million, as growth within our Route Based Services segment, inclusive of increased customers, volume, pricing and acquisitions, was partially offset by approximately \$5 million of additional short-term incentive accruals

that were triggered as a result of meeting certain financial targets, and over \$2 million of increased rate costs in the quarter.

I will go into greater detail on the growth drivers when I cover the operating performance of our Route Based Services segment, but the good momentum we saw in the fourth quarter in our Route Based Services segment gives us confidence in delivering on our full year 2019 targets.

Turning to cash, adjusted free cash flow from continuing operations in the quarter was \$65 million, which included working capital benefit. The working capital benefit we saw in the quarter resulted from an initiative we implemented to improve our working capital management. The initiative delivered \$25 million more in working capital benefit than we expected.

With respect to capital deployment, we returned approximately \$37 million to shareholders in the fourth quarter through \$8 million of dividends, as well as \$29 million in share buybacks. Of the \$29 million of share buybacks in the quarter, \$6 million of shares were acquired under the share repurchase agreement approved by our board in May 2018, and the remaining \$23 million of shares were acquired under the share repurchase program approved by our board in December 2018.

We also acquired Mountain Valley in mid-October, which provided approximately \$10 million of revenue during the quarter. We are excited to add to our portfolio this fast-growing, highly recognized American brand of spring and sparkling water. The transition and integration of Mountain Valley has gone smoothly, and we would expect to fully integrate this business into our Route Based Services segment over the next few years.

Moving to the full year, we saw good top-line performance across our Route Based Services segment, with consolidated revenue increasing by 5 percent at \$2.373 billion. Operating income grew 34 percent to \$59 million and adjusted EBITDA grew 6 percent to \$312 million, as a result of growth in

revenue and increased route density, partially offset by increased freight and transportation costs of around \$9 million. With good top-line momentum as we close the year, we feel confident in meeting our 2019 revenue target of over \$2.4 billion.

Turning to cash. Adjusted free cash flow from continuing operations for the year was \$150 million, which included approximately \$25 million of working capital benefits I just discussed.

With respect to capital deployment, we divested our traditional business at the beginning of 2018, which allowed us to de-lever our balance sheet by over \$1 billion through debt reduction. We returned approximately \$108 million to shareholders this year, through \$33 million of dividends, as well as \$75 million in share buybacks. And with the acquisition of Mountain Valley and Crystal Rock, in addition to several other smaller tuck-in acquisitions, we more than doubled our goal of 40 million to \$60 million of tuck-in acquisitions for the year.

And looking to 2019, we have the ability to deliver another 40 million to \$60 million of tuck-ins, as we continue to have a robust pipeline of targets, and we will continue to review other opportunities that would include companies of similar size as Mountain valley.

Let me now cover the operating performance of our Route Based Services segment. Looking at the fourth quarter, Route Based Services saw revenue increase 7 percent, 8 percent on an FX-neutral basis, driven by a positive mix shift in our North America customer base, growth in our overall customer base, and the benefits of our US 5-gallon bottle pricing initiative.

Our Route Based Services operating segment saw customers up 5 percent relative to the prior year, with volume up 4 percent, and average selling price per 5-gallon bottle up 3 percent in the quarter. Gross profit increased 5 percent to \$240 million, driven primarily by the revenue growth drivers I just mentioned, partially offset by the market inflation that we have discussed throughout the year.

Operating income was lower at \$7 million, as our growth drivers were more than offset by approximately \$5 million of additional short-term incentive accruals that were triggered as a result of meeting certain internal financial targets, and over \$2 million of increased freight costs in the quarter.

As we look to 2019, we are set up well for continued growth within our Route Based Services segment through our Customer 4 Life program, carryover of our pricing initiative, ongoing market growth as consumers continue to migrate toward healthy hydration versus sugary, sweetened beverages, as well as additional growth for our tuck-in acquisition program.

Let me now cover the operating performance of our Coffee, Tea and Extract Solutions segment. Looking at the fourth quarter, we continue to see top-line pressure from lower average cost of green coffee, which is essentially a pass-through item for us and does not materially impact our cash profits.

Excluding the change in average cost of green coffee, revenue was flat, as we saw our volumes stabilize, even with the competitive coffee roasting environment, as well as the difficult comps from lapping the outsized coffee and tea volume growth that we experienced in 2017 when we increased our market share and saw new customer pipeline fills. Overall, coffee and tea volume was flat during the quarter, while liquid extract volume increased by 4 percent.

Although gross profit was down year over year, operating income was \$4 million compared to 3 million, as the effect of a price mix shift into larger quick-serve restaurants was more than offset by liquid extract growth and reduced SG&A costs.

As we look to 2019, we are set up well for volume growth on a full year basis as we began onboarding a new national convenience retail chain in December, which will roll out over the course of 2019. We have also secured a number of new SKUs within our current customer base, driven in large part by our extract division, including a new cold brew coffee product, as well as entering into a new line of

service in which we have begun to assist a large, multinational quick-serve restaurant in Asia, all of which will come on board throughout 2019, which will result in a steady buildup throughout the year as the various contracts customers come on board.

With that said, the coffee roasting environment is very competitive. And although we have not lost any accounts as part of this process, we have had to sharpen our pencil a few times over the last year, while in turn working with both our customers and our team on cost-down measures.

As we move to 2019, we are set up well for volume growth and our full year expectations are very positive, but we will see some pressure during the first half of the year as the timing of a number of cost-down initiatives and new product launches slightly lag some of our pricing concessions. And in turn, we would expect to see some pressure on the top and bottom line in our Coffee, Tea and Extract business in the first half of 2019.

As a quick summary and looking out to 2019. Overall, in 2018, we had a good year where we delivered on revenue, EBITDA, and cash, while navigating through a variety of macro pressures. As we move into 2019, we have built momentum within our Route Based Services segment, where we have a number of growth initiatives working effectively, and a good pipeline of tuck-in acquisitions, setting us up well for 2019. And we have visibility into a number of new contracts and SKUs coming on board within our Coffee, Tea and Extract Solutions business, as we look to deliver on our 2019 goals, which incorporate top-line growth of 4 to 5 percent, as well as over \$150 million of adjusted free cash flow.

If you look at the deck that we posted, there is a slide that provides 2019 revenue and adjusted free cash flow expectations. And you can see that, when you exclude the sale of our RCI business that we announced a couple weeks ago, we are projected to deliver in excess of \$2.4 billion of revenue, or 4 to 5 percent revenue growth. This slide also shows how we plan to deliver in excess of \$150 million of adjusted

free cash flow in 2019, with top-line growth, interest savings, and synergies providing a \$20 million increase in adjusted free cash flow and tuck-in acquisitions providing an additional 5 million to \$10 million of incremental adjusted free cash flow.

This deck also shows the cadence of our revenue for 2017 and 2018. In looking at 2019, we expect Q1 will be a little lower and Q4 will be a little higher, relative to 2017 and 2018, based on what I just discussed with respect to our Coffee, Tea and Extract Solutions segment.

I will now turn the call back to Tom.

Tom Harrington

Thanks, Jay. As CEO, I will maintain continuity of our strategy and goals. I have been a part of this transformation over the last four years, and was a key member in the decision-making and development of the strategy and, therefore, I look at the transition as simply an evolution. With just three quarters under our belt since divesting of our traditional business, we've been able to display the attractive attributes of our improved business—one that has reliable, recurring, and predictable growth in revenue and free cash flow generation.

As we operate the business over the coming years, we will continue to focus on our growth and cash generation by:

One, becoming our customers' favorite direct-to-consumer service provider and premier water, coffee and filtration company, through an enhanced customer experience, which includes ongoing analytics of changing consumer behaviour, implementation of new and relevant customer touch points to our web and mobile platform, and instilling a service-oriented culture across our businesses.

Two, innovating with products and services across our leading platforms, through the utilization of current technologies that deliver the appropriate customer experience, as well as effective sustainability practices and stewardship.

And third, investing in our associates, the lifeblood of our organization, with effective development, career progression, competitive compensation, and the appropriate work-life balance, which empowers our associates to drive sustainable customer satisfaction and growth. I believe that we are positioned for growth well into the future, as we continue on our path of shareholder value creation.

Before moving to Q&A, I wanted to briefly touch on a few topics. The first is the information gap that exists within the market and who we are today; the second is our new environmental, social and governance, or ESG initiative; and the third is key initiatives for 2019.

Starting with the information gap. Consistent with comments that I made on our third quarter call, we continue to meet and speak with investors and analysts who mistakenly have considered us to be a soda company. And unfortunately, we continue to see ourselves grouped in with beverage companies, as opposed to business services companies. This is understandable, as we're in the early days of our improved business model. While this information gap can increase volatility in our stock price, it does provide a great opportunity to investors, as we continue to trade lower than our peer group within business services.

We remain committed to increasing our investor marketing and communication activities, where we will expand to geographies we have not historically visited, attend conferences that we have not historically participated in, and execute other outreach efforts as we look to educate the market on the fact that we are a different business, one that is part of the business service community, with products and services in growing categories, with lower customer concentration, reduced exposure to commodity

fluctuations, and one that has multiple levers to grow the top line, such as customer growth, tuck-in or customer list acquisitions, and improving customer satisfaction.

Moving to our ESG initiatives. Many of you likely saw the press release that we issued yesterday in which we announced that Shayron Barnes-Selby was appointed as Vice President of Government Affairs and ESG Programs, reporting directly to me, who will lead our ESG initiatives. Many investors are increasingly integrating ESG into their investment decisions, and we're currently receiving inaccurate ratings on our ESG scores from the third-party rating agencies, due in large part to information gaps with the information that they are utilizing. As a result, the development of an ESG communication program was one of my top initiatives to begin implementing, upon assuming the CEO role.

Although we will have a number of the program's goals that we will implement and achieve over the coming years, we now have a culture and operational expertise focused on social responsibility and sustainability, and already have many of the programs that investors look for when deciding to include a company in their indexes or funds associated with ESG. I see this as a seamless process, as the mind-set and the programs associated with these practices are embedded within our existing culture. They assist us in driving efficiencies, inspiring further innovation, and building platforms for long-term growth and assured supply.

With a number of programs already in place, we simply need to bring them to the forefront, and we've started to do so as our board's governance committee has taken on the responsibility of overseeing our company-wide ESG initiatives, and Shayron Barnes-Selby will lead these initiatives. Over the coming weeks, you will start to see more activity in this area on our website, marketing materials, and as a part of our presentations, all of which we believe will assist in creating further value for our Company.

Turning to some of our 2019 initiatives, I'm going to briefly cover our customers' experience service and growth' our US route based pricing initiative, and extract and channel expansion within our Coffee, Tea and Extract Solutions businesses, extracts, and Asia. So let's start with the customer initiatives within our Route Based Services segment.

Over the last few years, we have successfully implemented a number of initiatives to grow our overall customer base, while at the same time, focusing more effort in growing our commercial customer base. As a result, home and office water delivery customer programs have been executed to meet two goals: to drive total organic customer growth and to shift our mix of customers with a greater emphasis on growth of our commercial customer base. As we noted in our last quarter's call, we're pleased to report that our mix was now in line with our historical customer mix in North America. As expected, our total company-wide customer base ended the year at around 2.5 million customers.

As we look to 2019, our goal is to continue with our focused marketing initiatives designed to drive customer growth and improve our mix. These initiatives include: a continued investment in sales headcount, designed to improve our overall North America mix and to drive organic growth; continued investment and focus across our 20-country footprint on our website, the internet, and social media, in order to drive growth within our customer base and reach millennials and Gen Z-ers; and a continued focus on our high-density area, or HDA program, to improve the return and effectiveness of our custody marketing dollars, by focusing on a number of major urban markets where data indicates we can achieve a higher return from our sales and marketing investments.

Moving to our customer experience and service. We have spent, and continue to spend, a significant amount of energy and resources in this area, and it will continue to be a key area of focus in investment going forward. These activities assist in driving a lower quit rate, longer customer life cycle,

and supports our ability to drive organic customer growth and revenue per customer location. As we noted on our call last quarter, we continue to see a historically low churn rate in North America, and our European division continues to maintain a consistently low churn rate as well.

Customer-related activities will be a key topic when we hold our Investor Day on March 12th, where our North American Route Based Services management teams will provide a more in-depth discussion on these initiatives.

Turning to pricing. As many of you know, we rolled out a carefully planned and executed price increase initiative to our US Route Based Services customers. These various pricing actions have been phased in beginning in August, and were designed to fully offset the market inflation that has been present throughout 2018. I'm pleased to say that the pricing actions have come through as expected and were a key driver in offsetting around \$9 million of increased freight and transportation costs.

As we look to 2019, we will benefit by the rollover of these pricing initiatives, which in turn will continue to help us offset market pressures in the areas of increased labour costs, health and welfare costs, and company-wide investment, with the opportunity for some of the pricing to pass to our bottom line.

Moving to coffee, extract, and new menu initiatives, as well as our channel expansion projects. Our Coffee, Tea and Extract Solutions segment will focus on continuing to grow its core coffee and tea volumes, while seeing higher growth in product categories such as coffee extracts. We continue to build out our customers' menus in areas such as cold brew coffee and other extract-related products that have seen significant growth over the last few years, which we expect to continue going forward. We will be launching a number of initiatives in this area in 2019, which gives us confidence that we'll be able to meet

our growth expectations for this business. Extract volume increased by 30 percent in 2018, and we're expecting a similar growth profile in 2019.

Additional growth will come from our continued expansion into new channels that we've historically under-penetrated. A recent example is the assistance that we provided a large multinational quick-serve restaurant, where we leveraged our expertise to assume a coffee program in certain Asian countries. Although we are not benefitting from having this production within our plans, it was the ability to shift our customer with the process and the ongoing management expertise that will drive this channel's revenue, as well as further solidify us as an important partner with our customer. We've also seen our customers increase their orders of extracts for overseas shipments going into 2019.

Similar to our commentary last quarter, with key initiatives in high growth in the area of extracts and new channels, we would look for our core roasting ground coffee and tea business to deliver more modest performance, whereby collectively, we're able to deliver on our total volume and revenue growth goals across the business as a whole.

Before moving to Q&A, I wanted to take a moment to thank a number of individuals. First, Jerry Fowden, for all his efforts as our CEO during our transformation. His leadership and guidance were instrumental in navigating Cott and taking the business from one that had operated in categories in decline, with many macro factors that challenged the business, to a growth-oriented company focused on healthy hydration with predominantly recurring revenues and multiple scalable platforms.

During this process, we not only created a new business model, but we significantly improved our growth profile, shifted our emphasis and business towards Route Based Services, and meaningfully reduced our exposure to commodity fluctuations. Thank you, Jerry.

With the announcement of our CEO transition in August, we executed a seamless transition in roles for both Jerry and I, and we've hit the ground running in 2019.

Next, I would like to thank all the associates within our former RCI concentrate division. As you know, we announced the sale of these businesses just a couple of weeks ago, completing the transformation of our business. We wish them well.

And last but definitely not least, I would like to thank all of our associates, the lifeblood of our organization, without whom we would not have been able to accomplish everything we did in 2018, as well as everything we plan to accomplish going forward. So thank you all.

I will now turn the call back to Jarrod to move us to Q&A.

Jarrold Langhans

Thank you, gentlemen. During the Q&A, so that 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 for your time.

Operator, please open up the lines for questions.

Q&A

Operator

At this time, if you would like to ask a question, you can press *, and the number 1 on your telephone keypad. And we'll pause for just a moment to compile the Q&A roster.

And your first question comes from the line of Nik Modi with RBC. Your line is open.

Russ Miller — RBC

Hey, good morning guys. This is Russ Miller on for Nik. We wanted to ask first on—

Tom Harrington

Good morning, Russ.

Russ Miller

Good morning. We wanted to ask first on the 2019 free cash flow bridge. Are there any more details you can provide on the components of the bridge, such as core business growth synergies, tuck-in acquisitions? And all of these net of reinvestment back into the business? And what of these components present the biggest risk, or could lead to the most upside to the guide. And then I have a follow-up, if you don't mind.

Tom Harrington

Russ, I'm going to ask Jay to answer that question.

Jay Wells

Hey, Russ. I mean, I think what you're doing is, you're trying to take our previous bridge, add up the three parts of growth, interest, and synergies, to get to the new \$20 million on our bridge, is probably what you're trying to work through. And you really look at our old bridge, things that would have changed from that to the current bridge, first off, we did sell the RCI division. Within the synergy number that we had previously talked about, there was probably \$2 million of dis-synergies that we were going to capture and take out this year, which we will no longer see those since we have sold that division.

On top of that, of the interest savings that you've seen in the bridge, we're probably going to see maybe \$2 million less in cash interest savings in the year. So if you adjust those two numbers and add it up, you kind of get the 20 million in the middle of the range you would get. Is that helpful?

Russ Miller

Yeah. Thank you, Jay. And the follow-up question would be on Amazon. So we noticed Amazon posted on their Services website that they may soon be offering HOD water delivery services. Could you comment on this? And whether you see this as a threat or opportunity? Thank you.

Tom Harrington

Yeah, Russ, this is Tom. We actually view it, while not active, as another form of growth. So you thin, and we've articulated in the past, four or five ways that we'd pursue growth. There would be tuck-in acquisitions, it could be our investment in commercial ASRS, could be our in-store program. The Amazon opportunity, to us, is another way to attract customers, and frankly in a channel of business that might be new to us. So we would be cautiously optimistic about that opportunity and don't view it as a threat. We view it as an opportunity to expand the business.

Russ Miller

Okay. Thank you very much.

Tom Harrington

Thanks, Russ. Appreciate it.

Operator

Your next question comes from the line of Peter Grom with JPMorgan. Your line is open.

Peter Grom — JPMorgan

Hey, good morning, guys. How are you?

Tom Harrington

Good morning, Peter. Good, thank you.

Peter Grom

So just a few quick questions from me. So first, can you provide a bit more clarity on the increased incentive accruals? Maybe help us frame what was included in your original guidance versus the 5 million impact, and what drove the increased versus expectations?

And then second, just kind of following up on Russ's question, when we look at the 2019 free cash flow guidance, can you maybe provide a bit more colour on what could help drive the plus in your outlook going forward? Thanks.

Tom Harrington

No problem. I'm going to ask Jay to lead those answers.

Jay Wells

Morning, Peter. You look at the guidance we gave on the third quarter call, we gave a range of full year EBITDA of 312 million to 315 million. And when we gave that guidance, how we were trending on the pricing, we felt pretty comfortable that we were going to hit the higher end of that guidance, but also gave the range because we knew if we were able to exceed it and really over-deliver on our pricing initiative, there were certain thresholds that DS had not made yet on their annual bonus. So the good news is, we over-delivered on our pricing initiative. The good news is, our employees are getting rewarded for their very hard work, but also at the same time that additional accrual which we were able to do and provide to our employees, thanks to over-delivering, brought us down to the lower end of the EBITDA guidance.

Tom Harrington

And before Jay goes to the free cash flow, I just want to emphasize that paying out incentives for the work the team did with all the headwinds and the challenges they faced, we actually think it's important and sets us up, frankly, appropriately, to continue progress into 2019.

Jay, you want to take that?

Jay Wells

Sure. And on the free cash flow, opportunities for upside, well, you look at what we talk about will grow the top line, it's customers, it's price, it's consumption, and it's tuck-in acquisitions are really the areas of growth. So opportunities to over-deliver would be increased customer adds, increased consumption as people move to healthy hydration, and over-delivering on our current pricing initiatives I would say are key things. And then on top of that, we did two larger-scale tuck-in acquisitions last year with Crystal Rock and Mountain Valley, and to the extent we can deliver earlier on those synergies, that will provide upside.

Peter Grom

Great. I'll leave it there. Thanks.

Tom Harrington

Thanks, Peter.

Operator

Your next question comes from the line of Derek Dley with Canaccord Genuity. Your line is open.

Derek Dley — Canaccord Genuity

Hi, guys.

Jay Wells

Good morning, Derek.

Tom Harrington

Good morning, Derek.

Derek Dley

Just wanted to talk a little bit more about the Coffee and Tea Extract business. From what I understand, you guys were awarded a new coffee contract, a large coffee contract in Q4. I'm wondering, did that come in in late Q4 or in December and not have a huge impact on the volumes this quarter?

Tom Harrington

That's correct. It was late December, and it'll feather in over the course of 2019, so no big impact in the quarter and then a slow roll, if you think about it, as we move through the new year.

Jay Wells

Yeah. Keep in mind this isn't a customer going new into coffee; this is a customer transferring their production over to us. So it's only as each store needs new coffee and to refill, is when we'll start providing for them. So it really will be a slow rollout through '19.

Tom Harrington

And I think it's important to note, when we talk about new business gains and growth in our business, they are typically feathered in. So they don't all happen on Monday of week three, that they come over time as they get through the whichever customer supply chain, and ultimately through their stores, in many cases.

Derek Dley

Okay. That makes sense. You mentioned that you're witnessing a more—I think the term you used was more competitive coffee roasting environment. Can you just give us a little bit more colour on what you're seeing?

Tom Harrington

Well, it's, we've managed to hold onto our customers in our business, but we've done that at some lower pricing, based on the number of RFPs in the marketplace, so we've seen degradation in the

pricing. We kept the customer. We actually performed pretty well, frankly, in the fourth quarter, particularly as we think about where our extract businesses are going go. The good news is, we don't foresee many RFPs in the next year or so. So we're in a pretty good spot in terms of the future, as it relates to what has been arguably the historically most competitive market we've experienced.

Derek Dley

Okay. And is that one—is it driven by one of your larger competitors, implementing this lower pricing? Because from what I understand this coffee market historically had been very disciplined when it came to pricing.

Tom Harrington

We're not going to talk about any particular competitor, but most of the RFPs would have four or five roasters involved in that, and so that's really the landscape we're faced with. It's not always the same one; sometimes it's others. The fact is we have been faced with these challenges in a number of RFPs, and I think the team has done a terrific job dealing with that. Jay referenced better managing our costs, and the team did that to mitigate the margin pressures we had, that we will continue to see over the course of the first couple months as we build our pipeline and execute our plan.

Jay Wells

Yeah, but—

Tom Harrington

We remain confident—sorry, Jay—we remain confident in a decent year at S&D Coffee on a full year basis.

Jay Wells

Yeah. And I think, I want to reemphasize, and Tom said it, I mean you asked, is this one? I would say, no, it was—we have made sure we have secured long-term contracts with all of our major customers and do not see this reoccurring in the near term. So I think, as Tom said, we're set up well moving forward, but as I said, we did have to sharpen our pencils on some of these RFPs in order to make sure we lock in in the long term.

Derek Dley

Okay. And then just last one for me. Just in terms of the pricing, the 3 percent pricing that was implemented in the Route Based Service division, did you see any customer response to that? Or was it taken pretty well by your customers?

Tom Harrington

Yeah. I think the answer is, taken pretty well. And the best measure we have for that is, we have the best retention rate we've ever enjoyed and the lowest quit rate. So that's a pretty good indication of customer satisfaction and their ability to bear that price increase, so.

Derek Dley

Okay. Thank you very much.

Tom Harrington

Thanks, Derek.

Operator

Your next question comes from the line of Derek Lessard with TD Securities. Your line is open.

Derek Lessard — TD Securities

Hey, guys. Good morning.

Tom Harrington

Good morning, Derek.

Derek Lessard

Maybe just coming back to Derek's previous question on the extracts business. Over the last few quarters, you did have the significant growth there, and it was holding at 4 percent in Q4. Maybe can you just hit on what was the driver of that decline in growth?

Tom Harrington

Yeah. I would characterize it as timing, and that we've seen the business rebound early in the year with—back on pace, with 30-plus percent growth for 2019. So it's just a blip, it's time it came back, so we're pretty confident in how that business is going to perform.

Derek Lessard

Okay. And maybe just one for me before I re-queue. In terms of 2019 guidance, are you going to provide us with an EBITDA range, along with your revenue and free cash flow targets?

Tom Harrington

No. What we've provided is what we plan to provide. We've tried to demystify the cadence with the last two years of how it's performed, but our guidance will be confidence in 4 to 5 percent top-line revenue growth and confidence in 150-plus of free cash flow.

Derek Lessard

Okay. Fair enough.

Tom Harrington

Thanks, Derek.

Operator

Your next question comes from the line of Daniel Moore with CJS Securities. Your line is open.

Daniel Moore — CJS Securities

Tom, Jay, good morning. Thanks for taking the questions.

Tom Harrington

Good morning, how are you?

Daniel Moore

Good. Maybe it's rehashing, so I apologize, but maybe we can drill down a little bit into the cadence as it relates to H1 versus H2 for the coffee and tea business, kind of both top and bottom lines, key drivers there, and the confidence that you have in that coming back in the back half. And one follow-up.

Jay Wells

Yeah. Let me start, and I'll throw it out. Within my script, I did refer to the consolidated cadence that you will see, with fourth quarter of next year maybe being a 2 percent higher than the cadence we saw on those two years, and maybe Q1 being a couple of percent lower. That's all attributed to what we're discussing on the Coffee, Tea and Extract Solutions segment.

Tom Harrington

Yeah. And if you look at the full year, we're confident that the business will perform as expected.

Daniel Moore

Okay. And then in terms of Mountain Valley, still early days, but maybe just elaborate on any cross-selling or expansion opportunities that you've seen since closing there.

Tom Harrington

Yeah. We haven't implemented the cross-selling in a meaningful fashion. I will tell you, the teams are working on identifying what I'll call the white space inside the HOD system. So where are the areas

where we could sell and distribute Mountain Valley across the DS platform, that work is in active development, and we're quite happy with the early work and the performance of the business. The management team has stayed in place, and is going to continue to lead this great American brand on our behalf.

Daniel Moore

And lastly for me, Tom. In terms of the M&A pipeline, you mentioned opportunities of similar size to Mountain Valley. Are those predominantly in RBS? And any comments you might have around the opportunity set in route based North America versus coffee and tea versus Europe?

Tom Harrington

Yeah. So we have a good pipeline, particularly in RBS, so as I think about that pipeline and think of water and coffee, it's with a capital W. So that's our sweet spot. That's the best of our experience on both sides of the Atlantic. And we're pretty confident we'll be able to deliver our commitments on those tuck-ins, and all the benefits expected to come from that.

Jay Wells

Yeah. And before you drop off, Dan, I'm actually going to do a follow-up for Derek to provide a little bit of help. We have given free cash flow. The one follow-up call that—a question Derek didn't ask, well, do we have any CapEx or cash tax guidance. And our guidance for CapEx is 120 million, and our guidance for cash taxes is about 5 million. So those two types of guidance should help you out in your math. So didn't mean to trump you, Dan, but I just wanted to give Derek the answer to some of the things he might be trying to model.

Daniel Moore

Understood. Thank you.

Tom Harrington

Dan, did you get the answer there?

Daniel Moore

I think so. Yes. I appreciate the colour.

Tom Harrington

No worries. Thank you.

Operator

Your next question comes from the line of Mark Petrie with CIBC. Your line is open.

Mark Petrie — CIBC

Hey, good morning.

Tom Harrington

Good morning.

Mark Petrie

Good morning. I just wanted to ask about your assumptions for cost inflation heading into 2019. And that's been an area of, I guess, some surprise at different points, and I just wanted to sort of understand your assumptions there. And then your comfort with the current pricing that you've got in place, and the potential for other pricing actions through the course of the year.

Tom Harrington

I'll take the pricing part and I'll let Jay take your first question second. We're pretty confident in the pricing, so it's stuck. As we said earlier, we implemented in August, it was a slow roll, it was intended to cover that 8 million or 9 million of transportation costs, it did that. It continues to roll through. It should give us some benefit on the bottom line this year. It's in our plan. And, of course, we'll look for other

pricing opportunities throughout the course of the year, but we're pretty happy with the execution that we did, principally in the US-based route based system.

Jay Wells

And on the cost side, the good thing is, the business that we've become, we're a low commodity-risk business. On any type of resin, our bottles are used 60-plus times, so movement in that isn't a big exposure item for us. On fuel, we have an energy surcharge or similar programs throughout our footprint to offset that exposure. And I talked about the coffee in my prepared remarks, where it's basically a pass-through item to us that really doesn't affect our profits. So on the pure commodity side, we really have a small effect on it.

It really is looking at, Tom just mentioned, the transportation and freight costs. Keep in mind, 90, 95 percent of that costs are our route sales representatives, in-town drivers, mostly commission-based compensation, as we take price, as we grow, as we get more density, they get their raise. It's really much more related to the 5 percent that goes from plant to distribution centre, and that's where the high demand is for those drivers, and that's really what's created the bulk of the 9 million in headwind on transportation costs we've seen in the year.

We're still having to use some third parties as we have raised comp, we have increased our recruiting efforts, but we still have open seats, so we are still seeing the need to use third-party providers. We have secured some dedicated third-party lines to avoid the high real lever (phon) price, but we're continuing to see it. So will we see that same headwind next year? But we do see that we will see some, not as material as this year, but that's why we've taken the pricing, we've got the rollover benefit to offset that.

Mark Petrie

Okay. Appreciate the colour. Thank you.

Tom Harrington

Thanks, Mark.

Operator

Your next question comes in line of Amit Sharma with BMO Capital Markets. Your line is open.

Drew Levine — BMO Capital Markets

Hi, there. This is Drew Levine on for Amit. Thanks for taking the questions. So I first wanted to—

Tom Harrington

Good morning.

Drew Levine

Good morning. I first wanted to start circling back to Tom. You said that pricing began rolling through in August in a phased way, and I think, last quarter, the pricing impact had been 3 percent also. So just wondering if you could give any more colour on why that 3 percent number wasn't any higher this quarter.

Tom Harrington

Well, the 2 percent was the full year. So yeah, actually, it's moved the full year number because of that 3. I'd have to look back and see where we were in the first two quarters to answer that question. Our revenue is really the three components, which is a combination of how many customers you bring in, what's the consumption of volume growth and the price, and the price was more significant in Q3. It is only on 5-gallon, so it doesn't affect all of the products we sell. And it was only in the US, so it's a piece of a piece of our business narrowly focused, frankly, the pricing activity in August on the 5- and 3-gallon container in the US.

Jay Wells

And keep in mind, you are looking at the fourth quarter, which is a lower-consumption quarter for us. It's really the summer months where we see higher consumption. So the price did take effect in a lower-consumption month, so it wouldn't have as large of a component as you might think.

Drew Levine

Okay. And then there wasn't really much talk about this, but I think coolers got an exemption from tariffs. I know previously, you said maybe there was 2 million to \$3 million of additional CapEx from that. So wondering if that's any sort of benefit to 2019, if you get any sort of rebate from tariffs paid in 2018, and how we should think about that.

Tom Harrington

Yeah. So we did benefit on a portion of the tariffs which was specific to bottled water coolers that we have not yet got relief on any filtration coolers or parts, and we expect to get a rebate back from the federal government sometime this year for roughly \$2 million. And then the headwind is obviously going to be much lower than we had originally forecast, but we still see about \$2 million in terms of tariffs in 2019.

Jay Wells

Yeah. And I would not—within our current results, we did book the benefit of the tariff refund. So don't book a couple of million dollar benefit in next year's CapEx because we did book the receivable and the reduction of CapEx in the fourth quarter.

Drew Levine

All right. Thanks, guys.

Tom Harrington

Thank you.

Operator

Your next question comes from the line of Bryan Hunt with Wells Fargo. Your line is open.

Dave Cook — Wells Fargo

Hey, good morning. It's Dave Cook on for—

Tom Harrington

Good morning, Bryan.

Dave Cook

—it's Dave Cook on for Bryan. Good morning.

Tom Harrington

Good morning, Dave.

Jay Wells

Good morning, Dave.

Dave Cook

I just want to touch on, there's been significant press around slowing EU economies. Just curious to get your thoughts on that. I guess what if any sales trends changes has the Company seen in those EU markets, in the past couple quarters?

Tom Harrington

Yeah. We haven't seen any meaningful change in aggregate across the business in terms of top-line performance, so it's performed where we thought it would perform, at the end of the day.

Jay Wells

Yeah. I have not seen any softening in employment stats over in Europe, so that's one key thing we do watch. So employment levels still seem to be good and improving. And that part of our business is a much more commercial-focused type business, so we haven't seen any changes in the workplace that would affect our business over there.

Dave Cook

Gotcha. And then on—I guess my follow-up, I heard you mention the 40 million to 60 million of contemplated tuck-ins for '19. I guess, regarding your M&A strategy, is it fair to say that you're focusing on those tuck-in acquisitions while also keeping an eye on more transformational transactions? And then, I guess, where would you consider taking leverage up to for a highly strategic deal?

Tom Harrington

Yeah. Our focus is on continuing to hit that 40 million to 60 million tuck-in pipe, and we have a robust pipeline. I said earlier, it starts with a capital W. We've got actionable small targets we can execute, and will execute this year. We have remained very disciplined on our approach to any larger deals, and would not pull any transactions that don't meet our internal financial hurdles. And through '18, we didn't find anything that met the target.

Jay Wells

And we've talked before on leverage. Yes, for the right opportunity, we would take our leverage back up into the four times. But as we showed in the past, we would become fully focused at that point in time to de-lever the Company.

Dave Cook

Thanks so much.

Operator

There are no further questions in queue at this time.

Tom Harrington

Thank you.

Operator

I will now turn the call back over to Jarrod Langhans for closing remarks.

Jarrold Langhans

Thank you very much for joining our call today. This will conclude Cott Corporation's fourth quarter 2018 call. Thanks for attending.