Keurig Dr. Pepper
May 09, 2019
9:30 a.m. ET

Operator: Good morning, ladies and gentlemen, and thank you for standing by. Welcome to the Keurig Dr Pepper's earnings conference call for first quarter of 2019.

This conference is being recorded, and there will be a question-and-answer session at the end of the call. I would now like to introduce your host for today's conference, Keurig Dr Pepper Vice President of Investor Relations, Mr. Tyson Seely. Mr. Seeley, please go ahead.

Tyson Seely: Thank you, and hello, everyone. Thanks for joining us. Earlier this morning, we issued our press release for the first quarter of 2019.

If you need a copy, you can get one on our website at keurigdrpepper.com in the Investors section. Consistent with previous discussions, today, we will be discussing our performance on an adjusted basis.

Excluding items affecting comparability and with regard to the year-ago period, our financial performance also takes into account pro forma adjustments due to the merger. The company believes that the adjusted and adjusted pro forma basis provide investors with additional insight into our business and operating performance trends.

While these pro forma adjustments and the exclusion of items affecting comparability are not in accordance with GAAP, we believe that the adjusted and adjusted pro forma basis provide meaningful comparisons and an appropriate basis for discussion of our performance.

Details of the excluded items are included in the reconciliation table included in our press release and our 10-Q, which will be filed later today.

Here with me today to discuss our first quarter 2019 results and our outlook for the balance of the year are KDP Chairman and CEO, Bob Gamgort, and our CFO, Ozan Dokmecioglu, and our Chief Corporate Affairs Officer, Maria Sceppaguercio.

And finally, our discussion this morning may include forward-looking statements, which are subject to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements are subject to a number of risks and uncertainties that could cause actual results to differ materially.

And the company undertakes no obligation to update these statements based upon subsequent events. A detailed discussion of these risks and uncertainties is contained in the company's filing with the SEC. With that, I'll hand it over to Bob

Robert Gamgort: Thanks, Tyson, and thanks to everyone for dialing in. We got off to a good start in the first quarter. All four of our segments registered strong underlying net sales growth, and our brands continue to perform well in the market.

In addition, we drove double-digit growth in operating income, which, combined with significantly lower interest expense than last year and a reduction in our effective tax rate, enabled us to deliver adjusted diluted EPS growth of more than 30 percent.

The integration of the two legacy businesses continues to progress well and the strong financial performance during the quarter was supported by merger synergies, which as expected, began to flow through in a meaningful way.

As we've indicated previously, we expect $600 million of synergy capture over the next 3 years to contribute to EPS growth of 15 percent to 17 percent, while ongoing productivity will enable us to increase investment in the business to support continued top line growth.

Our cash flow generation remain very strong, enabling us to repay more than $400 million of debt in the quarter and continue to delever rapidly. Our confidence for 2019 continues to be high, supported by some exciting innovation in our Coffee Systems and Packaged Beverages segment hitting the market in Q2.

In addition, you've likely heard that we've made some moves in the energy space, having signed distribution agreements for Runa Clean Energy drink and Adrenaline Shoc, or A Shoc, a functional clean label energy drink. We also made a minority investment in A Shoc. Still early days, and we'll have more details to follow on our next call.

Turning now to the highlights of the quarter, starting with in-market results based on IRI. Retail market performance started off the year strong. We registered dollar consumption growth across our portfolio and grew our held market share in nearly every category.

Our CSD, premium unflavored still water, ready-to-drink coffee and shelf-stable apple juice portfolios all grew share, driven by solid performance of Dr Pepper and Canada Dry, for hydration, Peet's and FORTO ready-to-drink coffee and Mott’s apple juice.

In our U.S. coffee business, unit consumption of KDP-manufactured single-serve pods was essentially in line with category growth of 5 percent. And dollar share pods manufactured by KDP was 81 percent, down slightly versus a year ago.

While we generally don't talk about in-market results of our coffee business in Canada, it's worth pointing out that this business posted strong market share growth of 7.4 points to 68 percent in the quarter.

The strength was fueled by our new partnership with Tim Hortons, the leading coffee brand in Canada. In addition, given that we secured the license for McCafe pods beginning in 2020, we have great visibility to continued strong growth in Canada for the next 2 years.

Turning now to the financials on an adjusted basis. Our underlying net sales grew 2.5 percent, driven by growth in both volume and mix and net price realization. This excludes the two expected unfavorable impacts in our Packaged Beverages segment from the changes in our Allied Brands portfolio and a calendar timing that we discussed with you last quarter.

Specifically, on a year-over-year basis, the net change in our Allied Brands portfolio reflects evian, Peet's and FORTO now ramping up as compared to the established FIJI and BODYARMOR businesses last year that have since exited.

The second impact reflects unfavorable Q1 calendar timing versus year ago, resulting from the shift of Easter into Q2 and having 1 less shipping day in Q1.

Operating income grew nearly 11 percent or 260 basis points to 24.8 percent of net sales, primarily reflecting strong productivity and merger synergy, both of which benefited our cost of goods sold and SG&A. These positive drivers more than offset inflation, particularly in packaging and logistics.

Adjusted diluted EPS increased 32 percent to $0.25 in the quarter compared to $0.19 in the prior-year period. This increase was driven by the growth in operating income as well as lower interest expense and a favorable effective tax rate.

Turning now to our segments. I'll start with Coffee Systems. Net sales increased 1.7 percent, fueled by higher volume mix of 5 percent, partially offset by lower net pricing of 2.5 percent and unfavorable foreign currency translation of 0.8 percent.

This relationship between volume/mix and net pricing is consistent with our previously communicated expectations for strong volume growth to more than offset moderating price investment in pods to deliver revenue growth in Coffee Systems.

The volume/mix growth for the segment was driven by a 7 percent increase in K-Cup pod volume and a 12 percent increase in brewer volume, partially offset by lower pod shipment mix, driven by the growth of branded partners.

Regarding the strong brewer growth in the quarter, as discussed previously, we do not believe that brewer sales are an effective metric in predicting household penetration, which is the real driver of Coffee Systems because it doesn't capture the machine replacement cycle.

In addition, brewers do not behave like a traditional FMCG business, in that the timing of shipments does not match consumption well, especially on a quarterly basis.

Operating income for Coffee Systems increased more than 7 percent in the first quarter, reflecting the growth in net sales and ongoing productivity. We also recently began to realize merger synergies in cost of goods sold and logistics.

In the next several weeks, we will be launching our newest position to our brewer lineup, the K-Duo brewer. K-Duo provides consumers the ability to brew a large pod of coffee through a traditional drip system in addition to a single cup through K-Cup pods. The combination of these two technologies in one machine eliminates the need to have two different brewers on the kitchen counter.

K-Duo is the latest example of our robust, consumer-centric innovation program designed to drive new household penetration of the Keurig system by addressing, in this case, one of the top five barriers to system adoption.

The K-Duo is currently shipping to retailers, and we expect the brewers to begin reaching shelves over the summer, with the fall home entertaining and gifting season being the key time period for retail sale.

The K-Duo launch as well as the recently introduced K-Cafe and K-Mini will be supported with significant marketing investment across traditional and digital media platform.

Turning to the Packaged Beverages segment. Net sales for Packaged Beverages were significantly impacted by the expected unfavorable items discussed previously, namely changes versus year ago in our Allied Brands portfolio and calendar timing related to Easter and one less shipping day.

Collectively, these items amounted to a 6.6 percent growth headwind to the segment in Q1. Excluding these two items, Packaged Beverages' underlying net sales grew 1.4 percent in the quarter.

It's important to note that the Allied Brands impact will continue to be a headwind until the fourth quarter, when it will reverse to a positive impact versus year ago.

Driving the underlying net sales growth for Packaged Beverages in the first quarter were Core hydration, which continue to register exceptionally strong growth, with a nearly 60 percent increase in retail sales in the quarter, and Dr Pepper, reflecting the impact of higher pricing.

Canada Dry also performed well, successfully lapping its almost 17 percent net sales growth in the first quarter last year, driven by the launches of Diet Canada Dry Ginger Ale & Lemonade and Canada Dry Ginger Ale & Orangeade. Contract manufacturing also performed well in the quarter.

Operating income for Packaged Beverages was even with year-ago period, largely reflecting strong productivity and merger synergies, offset by inflation, particularly in packaging and logistics.

Looking ahead to the upcoming summer months, we're excited about the innovation plan for Packaged Beverages. We recently introduced a limited edition Dr Pepper Dark Berry variety in conjunction with Marvel Studios' Spider-Man: Far From Home movie that hits theaters in early July.

We also started shipping innovation behind Snapple namely 3 lemonade varieties. The innovation behind both Dr Pepper and Snapple is performing very well in the market in early reads, and we expect momentum to further increase as we enter the summer months and activate marketing support.

Turning now to the Beverage Concentrates segment. Net sales, which represents our sales of concentrates to bottlers and serves the fountain customers, increased nearly 5 percent in the quarter, driven by strong net price realization of 7 percent, partially offset by lower volume mix and unfavorable foreign currency translation.

The growth in net sales continued to be fueled by Dr Pepper as well as increases from both Crush and Big Red, the latter of which we acquired last year.

Operating income for Beverage Concentrates advanced 12 percent in the quarter, reflecting the strong net sales performance and timing of marketing investment that has skewed to the balance of the year.

Finally, turning to Latin America Beverages. Net sales for the segment increased nearly 3 percent in the first quarter, reflecting both higher net price realization and favorable volume/mix, partially offset by unfavorable foreign currency translation.

Operating income for Latin America Beverages in the first quarter was even with the year-ago period, reflecting growth in net sales, entirely offset by an unfavorable foreign currency transaction impact for packaging materials as well as inflation in input costs and logistics. With that, I'll hand it over to Ozan.

Ozan Dokmecioglu: Thanks, Bob, and good morning, everyone. I will start with a review of the financials for the first quarter, which was another good one for KDP. I will then transition to our outlook for the balance of the year.

Continuing on an adjusted basis, net sales for the first quarter decreased 1.1 percent to $2.5 billion compared to $2.63 billion in the prior year, which reflected a strong underlying net sales growth of 2.5 percent, driven by higher volume mix of 1.4 percent and a favorable net price realization of 1.1 percent.

More than offsetting this underlying growth were the expected unfavorable impact of 2.5 percent from changes in our Allied Brands portfolio and 0.6

percent from calendar timing. In addition, foreign currency translation was unfavorable, 0.5 percent in the quarter.

Operating income in the quarter increased 10.5 percent to $621 million compared to $562 million in the prior year. And on a constant-currency basis, operating income advanced 11.6 percent. This performance primarily reflected strong productivity and synergies in both cost of goods sold and overhead.

Partially offsetting these growth drivers was inflation in input costs, led by packaging, and also in logistics. On a percentage of net sales basis, operating income advanced 260 basis points in the quarter to 24.8 percent.

In terms of our segment performance for the first quarter, on an adjusted basis, net sales for Coffee Systems increased 1.7 percent to $968 million in the quarter.

This strong performance reflected higher volume mix of 5 percent that was partially offset by lower net price realization of 2.5 percent and unfavorable foreign currency translation of 0.8 percent. On a constant-currency basis, Coffee Systems net sales advanced 2.5 percent.

Operating income for Coffee Systems advanced 7.4 percent to $335 million compared to $312 million in the prior year-end. And on a constant-currency basis, operating income advanced 9 percent. Driving this performance were the benefits of the net sales growth and productivity.

As a percentage of net sales, operating income advanced 180 basis points in the quarter to 34.6 percent. As Bob mentioned, we are beginning to realize some merger synergies in the Coffee Systems segment in both cost of goods sold and logistics.

Turning to Packaged Beverages. Net sales for the segment decreased 5.3 percent in the quarter to $1.12 billion compared to $1.18 billion in the prior year, reflecting a combined 6.6 percent net sales headwind from changes in the Allied Brands portfolio that reduced net sales by 5.4 percent and calendar timing that reduced net sales by an additional 1.2 percent.

Importantly, underlying net sales grew 1.4 percent, driven by net price realization of 2.3 percent, partially offset by lower volume/mix of 0.9 percent. Also impacting the net sales comparison in the quarter was unfavorable foreign currency translation of 0.1 percent.

Core hydration, evian, Dr Pepper, Canada Dry and Xyience registered strong net sales growth in the quarter, along with growth in contract manufacturing, partially offset by declines in Mott's and 7UP.

Operating income for Packaged Beverages totaled $160 million in the quarter and was even with year ago.

Lastly, reflecting productivity and merger synergies. The productivity improvement included a $10 million net gain on an earlier-than-expected renegotiation of a manufacturing contract, which we were expecting later this year.

These positive drivers were offset by inflation in packaging and logistics. As a percent of net sales, operating margin advanced 70 basis points versus year ago to 14.3 percent.

Turning to Beverage Concentrates. Net sales for the segment increased 4.8 percent in the quarter to $304 million, driven by higher net price realization of 7.1 percent, partially offset by lower volume/mix of 2 percent and unfavorable currency translation of 0.3 percent. The net sales growth was fueled by Dr Pepper, along with increases in Crush and Big Red, partially offset by Canada Dry.

The shipment volume decrease for Beverage Concentrates was due primarily to Canada Dry, Dr Pepper and Schweppes, partially offset by higher volume for Big Red and Crush. In terms of bottler case sales, Beverage Concentrates decreased 1.9 percent, including fountain foodservice, which was 2 percent lower compared to the year-ago period.

Operating income for Beverage Concentrates increased 11.7 percent to $201 million compared to $180 million in the year-ago period, reflecting the benefits of the strong net sales growth and the shift of marketing into the balance of the year. As a percentage of net sales, operating margin advanced 400 basis points versus year ago to 66.1 percent.

Turning to Latin America Beverages. Net sales for the segment increased 2.7 percent to $116 million compared to $113 million in the prior year. This performance was driven by higher net price realization of 4.1 percent and favorable volume/mix of 1 percent, partially offset by unfavorable impact of currency translation of 2.4 percent.

On a constant-currency basis, Latin America Beverages net sales advanced 5.1 percent. Operating income for Latin America Beverages totaled $12 million and was even with the prior year.

This performance reflected the benefit of the net sales growth, offset by an unfavorable foreign currency transaction impact in the inflation in input costs and logistics. On a constant-currency basis, operating income advanced 1.3 percent.

Turning to interest expense. Interest expense in the first quarter declined $40 million to $131 million, reflecting a $27 million benefit from unwinding several interest rate swap contracts in the quarter and the benefit of our ongoing deleveraging.

As previously discussed, our interest expense outlook for the year is supported by our strategy to opportunistically use interest rate swap contracts to manage interest rate risk.

Net income for the quarter increased 35.4 percent to $356 million compared to $263 million in the prior year, driven by the strong operating income growth, lower interest expense and a lower effective tax rate resulting from U.S. tax reform enacted in December 2017.

Taking all of these factors together, our adjusted diluted EPS in the quarter increased 32 percent to $0.25 per diluted share compared to $0.19 per diluted share in the prior year. In terms of leverage, we paid down $414 million of debt in the first quarter, increasing the total amount of debt paid down in the 9 months post-merger close to approximately $1.35 billion.

We also have $85 million of unrestricted cash on hand at the end of first quarter. The debt reduction in the quarter, along with our growth in adjusted EBITDA, reduced our debt to adjusted EBITDA ratio, which we refer to as our management leverage ratio, by almost a half a turn in the quarter to 5.1x.

This aggressive pace of deleveraging is consistent with our expectations. And finally, in terms of our outlook for the balance of 2019.

For the full year, we continue to expect adjusted diluted EPS growth in the range of 15 percent to 17 percent, representing $1.20 to $1.22 per share, in line with our long-term merger target.

We continue to expect net sales growth of approximately 2 percent, which is also in line with our long-term merger target of 2 percent to 3 percent, and includes an approximate 100 basis points headwind impact from the changes in the Allied Brands portfolio. As discussed earlier, this headwind impacts the Packaged Beverages segment.

We continue to expect merger synergies of $200 million in 2019, consistent with our long-term merger target, and we continue to expect these synergies to fully flow through to EPS. We continue to expect interest expense to be in the range of $570 million to $590 million.

This reflects our expectation of significant cash flow generation and continued deleveraging during 2019 as well as the benefit of additional unwinding of interest rate swap contracts. We continue to estimate our effective tax rate for 2019 to be in the range of 25 percent to 25.5 percent for the year.

We continue to expect our diluted weighted average shares outstanding to approach $1.42 billion in 2019, including the 16.7 million of shares issued in November 2018 for the acquisition of CORE Hydration.

While we are not providing EPS guidance by quarter, we continue to expect EPS growth versus 2018 to be tempered in quarter two and quarter three due to comping the significant gains on Allied Brands in 2018 that we discussed last quarter.

We understand that modeling KDP as a new company can be challenging, so we share the following perspective for you to keep in mind when doing your modeling. We continue to expect our second-half synergies to be greater than our first-half synergies as our programs build throughout the year.

Based on our input cost coverage, we continue to expect inflation to be the highest in the first half and then moderate in the second half. And finally, in 2019, we continue to expect free cash flow to approximate $2.3 billion to $2.5 billion.

And we continue to be confident that we will achieve our leverage target of below 3x in 2 to 3 years from merger closing. With that, I will hand it back over to Bob for some concluding remarks.

Robert Gamgort: Thanks, Ozan. Before opening it up for questions, I'd like to provide some closing thoughts on the quarter. We started 2019 on a strong note and are on track to deliver our commitments for the full year.

Nine months into the combination of these two businesses, we remain confident in achieving our long-term merger target and the value creation framework we laid out over a year ago.

Our brands are performing well in the marketplace, and we continue to invest in innovation and marketing to ensure we position our brands and our company for future success.

Finally, the profit and cash flow generation of the new business remain strong, as evidenced by our synergy delivery, margin expansion and debt reduction. With that, I'll turn it back to the operator for questions.

Operator: (Operator Instructions). The first question will come from Judy Hong with Goldman Sachs.

Judy Hong: So Bob, I guess, I wanted to look at the pod growth in the quarter. And I know you talked about really focusing on the key metric, which is the category growth on consumption basis and then KDP-manufactured market share.

And I guess, both of those metrics kind of slowed in the quarters of category volume up 5 percent. Your market share was down a little bit.

So maybe if you can just provide us some context of what you're seeing from that perspective. And then as you think about some of the brewer innovations, how impactful do you think those could be this year?

Robert Gamgort: Yes. Thanks for your question, Judy. I see it as very steady performance on a business that doesn't fluctuate much quarter in, and quarter out. So on a 52-week basis, the category was up 7 percent. In the latest quarter, it was plus 5 percent.

I mean, that's all within the normal range of movement. If you look at our KDP-manufactured share, on a 52-week basis, it was just around 82 percent. On the quarter, as you point out, it was around just above 81 percent share, which we talked about was down slightly versus year ago.

If you look at the latest 4 weeks of IRi covering April, which we just got in, we're back up to almost 82 percent and we're up versus a year ago. So I look at the movements that you're talking about all within sort of the margin of error, and I don't see anything significant in those numbers at all.

Judy Hong: And then just in terms of innovation, how you think that could be -- how you see that is impacting?

Robert Gamgort: Yes. Our household penetration has continued to march up now on a nice pace, mid- to high single digits, for the past couple of years.

Innovation, marketing, in-store merchandising, addressing a lot of the barriers to household adoption. Price, for example, we talked about pods' price, of machines, quality of machines is up significantly, all of that combined is what's driving that steady increase in household penetration.

And our eyes are squarely focused on the 61 million households that we identified back in our investor presentation that are drip coffee consumers that really should be converted to single-serve.

And every piece of work that we do, whether it's brewer innovation or marketing or all the other pieces that I just listed there, are targeted at bringing those people in.

And it's going along very nicely. This latest introduction, the K-Duo brewer, specifically addresses one of the barriers to growth that we know that people have, which is a barrier to system adoption that people have.

I want to be able to make single-serve during the week, for example. On the weekend, when I have company over, I want to be able to make a large batch. I don't want to have two machines on the counter.

So for the first time, we're giving them a platform of multiple machines under this platform that allow them to do a full carafe of coffee using regular drip brewing process as well as a single-serve K-Cup with no compromise in quality, all in one machine. So all of this is what continues to drive that steady march upward in our household penetration.

Operator: The next question will come from Lauren Lieberman with Barclays.

Lauren Lieberman: I wanted to just talk a little bit, again, like longer-term for strategic vision. And I know part of the rationale for the creation of the company was filling in white space, capitalizing on kind of the scarcity value of the distribution assets that you now have. So you're kind of a year in.

I wonder if you could comment, one, on the ability that kind of stores' brands to fill in white space. And I know you've got the two new with Runa and Adrenaline Shoc, but those are arguably with existing relationships that you had with Lance Collins and buybacks.

So ability to store and then also on the distribution side, how effective do you feel your assets are versus competition, particularly when it comes to building out these sort of smaller challenging brands?

Robert Gamgort: Yes. I think in both cases, both in terms of our portfolio and in terms of our distribution and selling capability, I think one of the exciting parts about our business is how much opportunity for gain we have going forward.

One metric is to say, how good is our existing portfolio or how good is our existing distribution system today versus our peer set? But I think the more important metric for value creation is where do we think we can build from here and if we have more white space to fill.

You can see that when you take a look at our numbers, and we are going about doing that. And we have a great opportunity to continue to improve our distribution system, both in terms of its effectiveness as well as its cost structure. And you can see that starting to flow through as well.

So that's the exciting part of the opportunity going forward. Your point about sourcing new deals, I wouldn't dismiss the fact that the 2 new deals came in here are because of relationships. Relationships are really important in this industry, and they allow you to cut through a lot of noise.

And the fact that -- I'll just use A Shoc as an example. The fact that we were able to make the CORE acquisition, which was founded by Lance Collins, which continues to do incredibly well.

By the way, that business is now, if you look at the latest IRi, on a 52-week basis, it's $225 million. If you look at it on a run-rate basis, it's significantly higher, and it's still growing close to 60 percent. It tells you, that's a really good addition to our portfolio.

The fact that after we closed that deal, we were able to sit down and partner on an opportunity in an area where we have white space, I think, is a competitive advantage that we have, these strong relationships rather than going out there. And the last part I would say is we see a lot of deals.

The good news is we're in a position where a combination of our ability on improving our distribution system off of the strength that we already have, and the fact that we have white space is known by others. And so we get a steady inflow of ideas. The issue here is not, where do we source them from,

And which ones we choose to make sure that we don't overpay for anything today. I think the big shift that you're seeing with us certainly but with others in beverages, is there is no desire to pay these pretty high multiple sales.

We'd rather partner with people earlier in the process when things are more reasonable and grow the business together. So it's not about, are they available? It's a question, would they add value to our portfolio? And I think we are seeing this more.

Operator: The next question will come from Bryan Spillane with Bank of America.

Bryan Spillane: So a couple of questions. First, maybe a follow-up to Judy's question about innovation. Bob, can you just talk about -- initially, I guess going back a year or more ago, the first sort of wave of newer brewers was sort of lower price point, right, the mini, more entry-level price points.

If you're adding more premium price brewers, just some perspective on whether that's kind of activating higher-income households or just how that's tracking, right, so far.

Robert Gamgort: Yes. I think our ambition a couple of years ago, as you referenced, was, first of all, to introduce better machines across the board, both in terms of the quality as well as the -- do they deliver new features and benefits? And price point is critically important. So job one was to cover the price range.

So between the K-Compact, the K-Mini, as you referenced, all the way up to the K-Elite, we cover sort of the core, I'll call it, base Keurig brewer from a price point as low as $49 all the way up into around $150, $160. As part of the next move is to getting into new occasions.

So specialty coffee with the K-Cafe, the cappuccinos and lattes was really important for us. K-Duo is critically important. Because I said, one of the top five barriers to system adoption is the desire to be able to produce a large batch of coffee on occasion without having the machine.

So I think they cover the whole price range. And even you'll see, when we -- the K-Duo line is a line of actually three different brewers at a wide range of price points. So it's a combination of features, benefits, aesthetics, but also price point.

And we know, and we talked about this in our Investor Day back in March of 2018, we actually know that there's an opportunity in the high end of brewers, not just the low end, and that there are people who are willing to pay significantly more for a better-looking brewer and one that delivers additional benefits. And so we're filling in all of those areas of white space in our brewer portfolio.

Bryan Spillane: And then just maybe a follow-up on Lauren's question about sourcing deals. Does your ability to use equity, I guess, like you did with CORE, give you maybe a more attractive set of value options, I guess, for people who are looking to sell? Does that kind of give you an advantage in a way to -- the ability to offer some equity?

Robert Gamgort: I mean, it definitely does. A lot -- a number of people have said that we're probably out of the M&A game because we're focused on delevering and, therefore, we can't pick on more debt to make acquisitions.

And my first response is always we were able to do a great acquisition with CORE using our equity in a win-win scenario that was attractive to both sides.

So I think we have a lot of optionality for a deal. And again, what I reiterated, it's not an issue of being able to source deals. The real issue is, can we create win-win scenarios where we have a deal structure and a price point that allows us to create value, not destroy value.

And it's been fairly well documented. When you take a look at a lot of the big named beverage deals that trade at north of 5 or 6x sales, every single one of those has the destroyed value.

Even when it's a good brand, it's destroyed value because you can never pay that back. And look at CORE, for example. CORE is a business that's on fire. It's of scale already. When you take a look at it, we paid around 2x sales for that, and we used equity to do that.

That was a tremendous value creation mechanism. It was also strategically sound for us and a win for the seller as well. So again, we have lots of optionality. And the door's open. We're talking with lots of people as a matter of picking the right brands and the right partner to do business with.

Operator: The next question will come from Brett Cooper with Consumer Edge.

Brett Cooper: The coffee business seems to me is essentially a managed operation. I was wondering if you can talk about how you see running the ready-to-drink beverage business going forward, whether that business is managed more locally or regionally versus centralized and what that means for brand efforts in the introduction.

Robert Gamgort: Yes. I think -- so they're both a mixture of sort of central and sort of decentralized management. By its very nature, a DSD system, has a central component to it.

We're selling to -- for example, to national retailers that has to be all coordinated and have to be executed flawlessly in every retail outlet. So there is a heavy component that's centralized even within the DSD system. But to your point, the gamer end is won or lost store-by-store, shelf-by-shelf, day in and day out.

And with the DSD system, you have a tremendous amount of latitude to influence both merchandising and distribution at the local level. It's why we like it so much. That's why there are only a few systems, and we're one of them, that can get a single bottle or canned merchandise nationally in every small outlet in a cold format.

That is a very local action. So the real magic is a combination of a centralized decision-making with an execution force that can be coordinated locally. That's how sort of the magic happens.

Operator: The next question will come from Sean King with UBS.

Sean King: I guess, given the accelerated product cycle we're seeing in brewers, what sort of risk do tariffs pose? Are there any effort in place to kind of mitigate the risk there?

Robert Gamgort: Sure. So we watch this tariff situation closely. If you take a look at the next wave of tariffs that had been announced, because you've got to break them down to the individual items that are impacted, that one impacts our accessories and some warranty parts.

So at this stage, it's a minimal impact. We're talking less than $1 million. Now if that continues to expand, it starts to impact more and more of our business.

But at that point, it'd impact everything in the consumer electronics and appliance world. And I imagine there will be a price reaction. I mean, pricing will be taken in response to that.

But we continue to look for opportunities to diversify our supply base, and we've already done some to make sure we're spread -- our risk is spread geographically as well. So right now, we watch it. No immediate impact, and we're taking a lot of action to mitigate any future impact.

Operator: The next question will come from Peter Grom with JPMorgan.

Peter Grom: So I appreciate the color on your recent tricky partnership with investments, but on your outlook for these brands going forward. So the bigger picture question, obviously, under the category growth is very attractive.

So with greater compensation and category with bang and the Coke energy launch, how do you see these brands fitting in? So are they incremental to the category? And do you see them gaining share? Or do you think they're gaining share from the traditional players like Monster?

Robert Gamgort: Yes. The energy segment is attractive, both in terms of its absolute size as well as its growth rate.

And as the case in every consumer category where there's a large attractive segment, it begins to fragment until you start to break things out in terms of differential benefits, clean energy, more fitness-oriented energy. And that's the normal pattern you see in every large high-growth segment. And so the point is, we can be a player in that as well.

The important point to emphasize goes back to the distribution part of it, is brands are part of it, the equation. The other part of it is also distribution. And there are only a few systems of scale that can take advantage of putting those brands in the right point of distribution.

And we happen to be one of them. So it makes perfect sense for us to play within the energy space. And as I said a number of times, in a lot of these large, fast-growing attractive categories, we don't have to be the #1 or even #2 player in some of these segments.

We just have a meaningful business that's incremental to our portfolio, that allows us to participate in these really attractive categories. And energy is an area where we have a lot of white space. And therefore, we view that as truly an opportunity for future growth, which is why we're entering this with multiple players.

In addition, by the way, we talked about A Shoc and Runa today, but remember, we also have FORTO energy shot. We also acquired this Xyience brand as part of the Big Red acquisition, which is growing really nicely right now off of a relatively small base.

But in terms of growth, they're doing quite well. And so we look at any space like energy as an opportunity to attack it with multiple brands and multiple ideas to be able to get our fair share of that segment.

Operator: The next question will come from Bill Chapell with SunTrust.

William Chappell: Just going back to the pod sales in the quarter and kind of the mix. I guess, one, can you just help me understand where we are in terms of the price negotiations from a year ago? Have we fully lapped that going forward?

And then second, how should we look at the health of the company-owned brands? I mean, I understand the mix is going to naturally be like -- declined or be more towards distributor brands, but do you see that changing? Or do you see this trajectory changing at all as we move through this year?

Robert Gamgort: So let's start with the pricing piece of it. As we talked about, in the past year, that we should expect pricing to decline, and we said that would happen for a couple of years.

And it's not -- one of the things that I'd like to comment on is it's not something that surprises us. It's totally expected, and it's part of our strategy even more importantly. So we've driven significant productivity, which we reflected in pricing to our partners, which has allowed us to sign multiyear contracts with all of them.

And it's also allowed the pricing to be passed on to the consumer, which addresses the number one barrier -- previously was the number one barrier to household penetration, which was the price of pod.

So this is all part of the strategy for us. And you can see the fact that this was an intentional part of our strategy by two metrics. Category is growing, our KDP-manufactured share's very healthy at 82 percent and the margin in our Coffee Systems continues to grow despite the pricing.

So those are all the sort of proof points I would give that this is not an accident, this is part of a broader strategy. Having said that, we talked about moderation and pricing over time, and you're seeing that happen.

So if I take a look at KDP-manufactured price at retail as an IRi metric, $0.52 a pod, that's down from $0.53 a pod, which was the case for almost all of 2018. So you're talking about a $0.01 drop over a year on that. Where does that come from? If you actually go and look at it in detail, you'll see brand-by-brand.

The brands aren't dropping their prices. You're seeing slightly more mixed going towards private label, which is inherently lower price, therefore, it's diluting sort of the overall price.

But it's not people -- individual brands dropping their price. It's more of a mixed piece of it. And the other element that's happening is as this category gets more established, we're all shifting our packs to larger sizes, which makes sense.

With the amount of consumption that goes on and the number of households now that have a system, buying a 10 or 12-pack of pods doesn't make sense anymore. So you're seeing a big -- a shift to bigger pack, which, on a per pod basis, actually reduces the price slightly, but from a margin standpoint is a win for everybody.

I don't see the retail price as really a significant negative. And as I said, of course, it's all expected. The other thing I would point out, too, as we said before, we have multiyear contracts with a great majority of our partners.

So we actually know what our pricing is to them for the future. And you're starting to see that as well. The other metric you can look at is with our own quarterly releases. You can see the pricing headwind that would be in our net revenue line.

And about a year ago, that was a 6.5 percent decline. If you look at it by the end of the year, it was minus 3 percent. If you look at this quarter, it's minus 2.5 percent. So everything that we've been saying in the past year or so is all coming true, which is moderation in pricing and everything else moving in the right direction.

It's going to continue for a period of time, and that's -- we've been consistent on that. And it's not like, OK, that's over with this year. It's going to continue for a period of time, but everything else is exactly as we described.

William Chappell: And then just to follow up -- the second part of my question, the company-owned brands, the health there and what you're doing, and I understand you're relatively agnostic, but, I mean, I imagine you still make a little better penny profit. So just trying to understand kind of how that -- how you see that or what you're doing to maybe stabilize that, if anything.

Robert Gamgort: Yes. And actually, it has more of a revenue impact than a profit impact. And the reason is, when we sell a company-owned brand, we get -- we reflect revenue of everything in that brand.

Whereas when we sell a partner brand, in some cases, we're only reflecting the revenue we get for converting the pods for them. So it has more of a dilutive impact on revenues than anything else. And remember; when it's your own brand, you also have to apply overhead and marketing expenditure to it.

So that's why we say from a profit impact, we're more agnostic. From a revenue standpoint, it has more of an impact on us. Look, where we sit here today is we manufacture 82 percent of the pods that are in the marketplace right now. That's the most important metric of all.

And the composition within there has shifted slightly. Our owned and licensed business is around 23 percent of all pods sold. Our partner's about 50 percent of the market, and then we produce private label that represents about 9 percent of the market.

The fact that the owned and licensed side is declining a little bit right now is all sort of part of our greater strategy. And as I always point out to people, at one point, we had 100 share. And so as we continue to add more brands, including private label brands, to the marketplace, it causes the system to grow, but it dilutes our share.

And that's been going on in this business since the beginning, actually. And if you go back -- and, look, there were years from 2014, 2015 when the share loss was greater than it is right now.

Operator: The next question will come from Bonnie Herzog with Wells Fargo.

Bonnie Herzog: I just -- I wanted to circle back to your legacy Dr Pepper portfolio with a couple of questions. First, how does your innovation pipeline for this business look this summer compared to last year? Is there a significant step-up?

I guess -- and I have a sense from you guys that you thought this was a big opportunity. So I kind of wanted to hear how much progress you've been making there. And then on price realization in Package Bevs, you did see an improvement in the quarter.

So I wanted to get a sense from you on how sustainable you think this is. And maybe the elasticity and possibly how much more room you see to take further pricing as well as maybe opportunities to push further in the small package sizes to drive better price realization and top line.

Robert Gamgort: All right. Let me talk about the innovation piece first, then I'll come back on the pricing piece. On the innovation front, as we talked about on the call here, we've got last year a really strong year on Canada Dry.

The business has grown about 15 percent, partially driven by innovation of Canada Dry, Ginger Ale & Lemonade, which continues to be strong this year. But also just based -- growth on the base Canada Dry business, driven by a lot of good things, including some very good marketing behind that.

That continues into this year, and we're introducing now a diet version of Canada Dry Ginger Ale & Lemonade, which was a request from consumers and retailers based on the success that they saw.

And then we're introducing a Ginger Ale & Orangeade version of that. We've got a limited edition version of Dr Pepper. You're seeing limited editions do well in the marketplace. And clearly, there's good social media buzz right now going on at Dr Pepper.

We're seeing a bunch of variants increasing on our Snapple business, lemonade-focused. And even the Sunkist brand is doing quite nicely right now behind innovation. So we're really pleased with the level of innovation that we see on CSDs.

We've got a strong pipeline that will continue going forward. And you see it in the fact that we continue to gain market share on our total CSD business, which is probably one of the most important indicators.

In addition to the innovation on our own portfolio, remember, we're still in the very early stages of a number of our new partner brand agreements. We're just ramping up evian as we speak.

Peet's and FORTO are growing nicely right now, again, very early days on that. And then we just talked about some of the energy deals that we've entered into. So our team is really busy out there. They've got a lot of innovation to sell.

And the traction is -- all of that innovation that's getting in the marketplace is really encouraging. To talk about the pricing side, if you take a look at where we were in the fourth quarter, which we discussed on the last call, the category of CSDs I'm talking about now was up about 6 percent in price.

And we were up about 6 percent in price. The difference was our elasticity was significantly better than the category. So the volume loss that we saw associated with that price increase was about half the level that the category saw.

And that's why we were gaining share nicely at that point. If you look at the first quarter, you see that it looks -- if you go on the IRi or Nielsen numbers, it looks like our pricing actually went up fairly significantly versus the fourth quarter.

In fact, IRi shows our pricing up 7.5 percent. That is specifically related to timing and strategy around certain promotions. And I could even pinpoint it down to certain pack sizes and certain geographies where you see a very significant increase in year-over-year pricing.

That's 100 percent due to change in some tactics and timing around promotion. If you look at the Easter time period, it continued. We were up 6 percent. Category was up 3.5 percent. So we were way above the category on pricing.

Again, it's all promotion. And we were up 6.5 percent in revenue during the Eastern time period. So we're pleased with where we're at. The pricing is obviously -- there's no concern about its sustainability. It's clearly sticking.

And we're growing revenue and share as a result, but there'll be some recalibration on our promotions from time-to-time as we dig into this and understand sort of promotion returns and effectiveness even better. We're doing a lot of fine-tuning on certain packs. Your point about small packs, the whole industry is doing well on small packs.

We have a significant amount of upside to get more brands and more distribution on that. And that's good from a consumer standpoint. It's good from a pricing and profit standpoint as well. So we still have a lot of runway in front of us on that opportunity.

Operator: The next question will come from Amit Sharma with BMO Capital Markets.

Amit Sharma: Bob, can you just, in response to Bill's question, that was a really helpful discussion on the pod pricing and the mechanics, right? Just on that topic, one of the things you said was brands are not dropping prices. And that's clear looking at the IRi data.

But the question is that, look, if category volumes that have softened a little bit, if they continue to soften, should we worry about brands becoming a little bit more right about those volume decline and then start to drop prices or at least ask you for a little bit more on the pricing front. And that accelerates the pricing declines that you expect to moderate from here on?

Robert Gamgort: Yes. I will talk about sort of brand pricing dynamics, I don't want to talk about a hypothetical if categories starts to slow because we have no indication of this.

And the fact that we're plus 5 on a quarterly basis versus a plus 7, I think that's all noise, to be honest with you. We don't want to react too strongly to those kind of numbers quarter-to-quarter.

I think if you take a look at what's really interesting within the pod business, there's a lot made about growth in private label, which is fine. It's an entry-level price point for consumers. It brings them into the system.

It's the brand's opportunity now to trade people up to their favorite brands at higher quality to pay more premium price on that. But that's where lot of -- I see a lot of the reporting on.

What gets missed in that conversation is what's also growing significantly in the pod category is the premium-priced brands. Those brands that are still priced close to $0.70 are still growing and gaining share within the system.

And you're not seeing really any reduction in price at the premium level at all. In fact, you see some brands actually in the last quarter went -- is due to promotion, went up slightly in price. So it tells that you're getting all kinds of consumers into this system.

You're getting people there very price-sensitive. You're also getting people now who recognize the quality and are willing to pay for it and look for their favorite coffee shop brands in a pod as well. And in that segment, you've got Peet's. And Starbucks and Dunkin are in there.

And they are -- collectively if you add them up, they're all growing share as well. I think it's a very healthy situation in the pod market. And you're seeing it start to settle out in this sort of good, better, best pricing structure that you see in almost every category.

Amit Sharma: Got it. And then one quick for Ozan. Ozan, interest expense came in well below our expectation, and The Street was a little bit higher, too, but you're keeping your full your interest guidance unchanged. Are you expecting it to trend up higher as we go through the quarters? Or will it remain higher?

Ozan Dokmecioglu: Yes, we are keeping our full year guidance that we've put out there a couple of months ago. And the reason, maybe you see quite a bit favorable as well as lower interest expense versus last year. As we have disclosed, there's a good healthy interest rate swaps that we have unwound in quarter one.

Obviously, we had some plans with regards to the unwinding throughout the year, but as you know, we need to react how the market provides the opportunity or the other way around for us.

And we saw a good opportunity, and we unwound the healthy track of interest rate swaps, which took it lower than on an expected basis maybe. But our full year, either the unwinding or the estimate on the interest rate as well as the interest expense does not change.

Operator: The next question will come from Nik Modi with RBC.

Sunil Modi: Two quick questions. On the evian business, Bob, maybe you could just talk about -- my understanding is FIJI's having some issues that they've gone self-distribution.

They were a lot of out-of-stocks, so just wanted to get an update on evian and kind of how you're seeing that play out. And if you're actually seeing that at retail? And then -- second thing, it's on the brewer innovation.

One of the things you talked about, as you're launching some of these new systems, was you're looking to expand the demographic rings of the portfolio, particularly with the more affluent consumers. And so I'm just -- I was hoping you can give us an update on that.

Robert Gamgort: Sure. On the evian business, again, we're -- evian is a little different than a Peet's or FORTO or an A Shock in that it was a going business.

So what's happened over the past quarter is we're taking over responsibility for that brand at the large customer level as well as building the distribution at the small outlet level. And so if you take a look at total distribution before and after, it's about the same.

But if you take a look at small outlet that you can track, you see a steady increase in the distribution availability in convenience stores, and then we have a separate metric that we take a look at because it's not available and syndicated, which is up or down The Street accounts, where we're getting distribution.

And we're seeing a really nice build on the small outlet distribution of evian. And then, again, back to your point earlier about sort of water brands in total, I've said a couple of times, it's really hard to get that store-by-store distribution, especially up and down the street merchandise coal.

And it's really Coke, Pepsi and Keurig Dr Pepper that are capable of doing that. And that's why any brand that works its way into those three systems, who previously didn't have that capability, is going to see a gain in distribution and sales growth as part of that.

So again, still early days for us on evian, but we're pleased to see in a small outlet areas, in particular the distribution. And we're very bullish on that brand going forward. With regard to brewer innovation, yes, we're seeing all demographics coming in.

And if you take a look at sort of what is our opportunity set right now, we talk about more than 60 million households, there's a wide range of income that goes within those segments. And we've got brewers that are at the $50 price point now all the way up to around $200 or even slightly north of $200 coming out with some of the new items.

And it attracts a wider range of demographics into our system, which we think is good. I think that's also partly reflective of why the premium segment, as I pointed before, the most expensive pods in our system are actually growing in the absolute and gaining market share.

And I think it's also reflective of a higher-end consumer with more appreciation for quality coming in to the Keurig system. So again, all part of the strategy, and we're excited with the progress that we're making there.

Operator: At this time, I would like to hand the conference back over to management for any closing comments.

Robert Gamgort: Thank you, everyone, for dialing in today. We know that we weren't able to get to all the questions, but the IR team is around all day today. So feel free to give us a call, and we look forward to talking. Thanks, everyone.

Operator: Ladies and gentlemen, thank you for participating in today's conference call. You may now disconnect.

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