Here’s 1 Addictive Company That’s Heading in the Right Direction

Description

I’m always on the lookout for new stocks to put in my dividend portfolio. After pouring through the TSX listings, I came across one company that I have seen in the past, but which has never jumped out at me before. Perhaps it is the fact that I am sipping on a cup of life-giving coffee that made it seem more appealing, but **Cott** (TSX:BCB)(NYSE:COT) suddenly appears more attractive as an investment. I decided to take a deeper look at this company to determine whether it was actually a good business to add to my dividend portfolio, or whether it was just my early morning coffee addiction that was drawing it to my eyes.

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For those of you who have not heard much about this company, Cott traditionally was a carbonated beverage manufacturer. In 2017 it sold that business for US$1.25 billion to pay down debt and move in a new strategic direction. The company has recently adapted its business model to focus on water, coffee and coffee extracts, tea and filtration solutions. These products are delivered in a direct-to-consumer format in North America and Europe, where the company operates.

While its change in strategy is interesting, it also raises the question of whether the move is going to be profitable and a worthy investment in the long run. The company has taken on a lot of debt since 2014 to fund its acquisitions responsible for the change in strategy. Purchases of companies like the U.K.-based Aimia Foods and the U.S.-based DS Services have made the strategic, direct-to-consumer transition possible and have led to a significantly leveraged balance sheet.

What needs to be seen is whether the strategy translates into revenue, earnings, and free cash flow growth. In the second quarter of 2018, Cott reported 4% year-over-year revenue growth — a move in the right direction considering its revenue had been contracting for a couple of years. It also reported a positive net income of US$0.08 as opposed to a loss a year earlier. While it is still too early to tell if the company will continue to improve, it is moving in a positive direction. The company also pays a small dividend of 1.61%, which has held steady as the company undergoes its strategic transition.

For those of you who consider environmental impacts rather than just pure financials when you invest, Cott has a couple of other interesting points. Its European operations are 100% powered by green energy, for one thing. It has also been working to reduce the plastic used in its Canadian and U.S.

branded bottles by 50%. It has also created Raíz Sustainability®, a sustainable sourcing program used to help small farmers in several countries.

Cott’s business model as a direct-to-customer service is a good idea, especially at a time when soft drinks have somewhat fallen out of favour. Its water, coffee, and tea products will most likely be in demand for some time. The biggest issue is its debt. While you could argue that it used its debt to make accretive acquisitions at an opportune time in the business cycle, I would like to see the debt start to come down a bit, preferably paid down by free cash flow as opposed to asset sales.

It would be a good idea to continue to monitor the company’s progress. It’s becoming more geographically diversified over time, which is appealing. I think the important fact to keep in mind is that Cott at this point is essentially a new company considering its acquisitions and the sale of its legacy business. I like the new business, and its environmental focus is appealing, but I think I will treat it as a new, growing company and wait to see how the transition goes before getting into Cott.

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