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CORPORATE PARTICIPANTS

Kate White
The Stanley Works - Director of IR

John Lundgren
The Stanley Works - Chairman & CEO

Jim Loree
The Stanley Works - COO & EVP

Don Allan
The Stanley Works - CFO & VP

CONFERENCE CALL PARTICIPANTS

Sam Darkatsh
Raymond James & Associates - Analyst

Nigel Coe
Deutsche Bank - Analyst

Eric Bosshard
Cleveland Research Company - Analyst

Ken Zener
Macquarie Research Equities - Analyst

Michael Rehaut
JPMorgan Chase & Co. - Analyst

Peter Lisnic
Robert W. Baird & Company, Inc. - Analyst

PRESENTATION

Operator

Good morning. My name is Sarah and I will be the conference operator today. At this time, I would like to welcome everyone to The Stanley Works third-quarter 2009 results conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. (Operator Instructions). Thank you.

I would like to turn the call over to Kate White, Director of Investor Relations. Ms. White, you may begin your conference.

Kate White - *The Stanley Works - Director of IR*

Thank you so much, Sarah. Good morning, everyone, and thank you all for joining us on The Stanley Works third-quarter 2009 conference call. On the call in addition to myself is John Lundgren, Stanley's Chairman and CEO; Jim Loree, Stanley's Executive Vice President and COO; and Don Allan, Stanley's Vice President and CFO. I would like to point out that our third-quarter earnings release, which was issued this morning and a supplemental presentation, which we will refer to on the call and are on the webcast, are available on the brand-new Investor Relations portion of our website, www.stanleyworks.com.

This morning, John, Jim, and Don will review Stanley's third-quarter 2009 results and various other topical matters followed by a Q&A session. The entire call is expected to last approximately one hour and a replay of the call will be available beginning at 2 PM today. The replay number and access code are in our press release, and as always, please feel free to contact me with any follow-up questions after today's call at my number, which is 860-827-3833.

We will be making some forward-looking statements during this call. Such statements are based on assumptions of future events that may not prove to be accurate, and as such they involve risk and uncertainty. It is therefore possible actual results may differ materially from any forward-looking statements that we might make today, and we direct you to the cautionary statements in our 8-K, which was filed with today's press release and our most recent '34 Act. With that, I will now turn the call over to our CEO, John Lundgren.

John Lundgren - *The Stanley Works - Chairman & CEO*

Thanks, Kate, and thanks for all of you on the phone for joining us this morning. Let me spend a minute on the state of Stanley in terms of an overview.

First of all, we reported third-quarter diluted EPS from continuing operations of $0.77 a share. Regrettably in reporting our results, one or two of the news agencies dropped this number, which was actually in the headline of the press release we issued this morning. So some of you may have had to search the text in our exhibits a little more than we intended. But it's $0.77 EPS, very clear and straightforward, which compares to $0.97 a year ago from continuing operations 3Q '08, and on a GAAP basis, the $2.04 that we recorded last year included $1.07 gain on the sale of our CST laser measuring business. Hopefully all that is clear and we can move forward from there.

We are still experiencing mid-teens volume and revenue declines versus a year ago, but we're encouraged by modest sequential revenue growth in the third quarter given the lack of seasonality in our business. We were even more encouraged by margins, a record quarterly gross margin of 41.3%, which was achieved due to good pricing discipline, as well as some meaningful cost productivity initiatives. Commodity deflation, which we are experiencing, was essentially offset by the impact of the volume under absorption. So those, in a sense, offset one another on an equal basis.

Cash flow was also encouraging, $158 million for the quarter. That was up $55 million versus the same period year ago as we continue to execute our Stanley Fulfillment System and that process and program gains traction. As a consequence, we're able to raise our cash flow guidance for the year and we now expect to exceed $300 million in cash flow.

Security segment achieved a 3% revenue growth and a 13% profit growth versus prior year, and within our Convergent or electronic subsegment, organic revenues increased 5% sequentially, which is also encouraging given the state of the market.

CDIY did show signs of sequential demand stabilization around the world. The focus on going forward, particularly in the fourth quarter, is going to be new product rollouts, which we tend to do twice a year in waves, normally in the second and fourth quarter, to stimulate further demand. As a consequence of third-quarter results, as well as our assessment of the environment over the next two to three months, our full-year EPS guidance has also increased to a range of $2.84 to $2.94.

Taking a geographic look at revenues, all major regions continue to absorb double-digit declines, which is indicative of the weakness in global economic conditions. The US, which accounts for nearly 60% of our revenue, was down 17% organically and 16% in total. Europe was off about 22% organically, 16% in total as acquisitions played a role there, as well as Asia and Australia down similar measures. So no particular large geography in terms of our revenue was affected more than the other. It's a fairly broad-scale softness, which I'm sure you have heard on many calls, and Don is going to talk a little bit more about what we're experiencing later.

In terms of our third-quarter results per se, operating margins rose 40 basis points to 14.4%. You can see the EPS of $0.97 that I referred to a year ago versus $0.77 this year. Tax rate was favorable by 240 basis points, 22.2%, and we were a little bit affected by share count being up marginally, up 800,000 shares to 80.6 million. So pretty straightforward in terms of EPS. Reasonably a strong performance despite the continued volume headwinds, which is obviously having an impact.

Looking at revenues for the third quarter, as mentioned, they did improve sequentially to $936 million from $919 million in the previous quarter, but importantly, were down 16% versus the same period year ago.

Looking at the left of the chart in terms of sources of growth, as mentioned, volume is down 20%. We got some help from price with continued discipline of 2% favorable, so that's the organic 18% revenue decline to which we referred. Currency was negative, but less so than in previous quarters, as you can see the trend as the dollar strength changes relative to foreign currencies. And acquisitions was positive, but that was also less help than in previous quarters. It added 4% to our total revenue base versus 7% and 6% in prior quarters. So in total, revenues down 16% versus the same period year ago.

Looking at the segments, I won't spend too much time on revenue because Jim is going to take a much deeper dive into that a little later on in the presentation. But it's clear from this segment chart that our industrial businesses around the world are under the most pressure in terms of revenue. CDIY is still experiencing external headwinds, but certainly it appears to be abating to some extent. And security is holding up pretty well under the circumstances and obviously contributing to some of the stability that we're experiencing.

Moving onto volume trends, they are stabilizing to some extent. That's due in part to simply the mathematics of weaker prior year comps that are present, beginning 2Q '09, which was essentially the beginning of the downturn. The chart I think is fairly straightforward where you see our third-quarter unit volume down 20% and revenue's down 16%, as I suggested, and those comps will be a little easier, a little more favorable in the fourth quarter as we look to close out the year.

We were encouraged by our working capital performance, despite a 16% revenue decline. Our turns improved 8% as previously mentioned, as the Stanley Fulfillment System gains further traction. We took 3 days out of inventory versus same period year ago. 9 days out of receivables. Payables were unfavorable by 7 days. The negative impact is due to a combination of lower volume, less CapEx, and in some cases concession on terms as we leveraged our strong balance sheet to get more favorable discounts and prices based simply on an ability to pay our bills on time, and supplier credit is always good to have. So are large discounts when you're able to achieve them. So in total, we have seen turns improve from 4.8% to 5.2%, which, as Don has talked on previous calls, is a tremendous source of cash flow.

Finally, last but not least for my piece, a minute on our record gross margins of 41.3% and very strong operating margin of 14.4%, which hopefully this chart indicates is not a short-term phenomenon. A lot of things going on to achieve this as well as the cash flow, especially within our core businesses. It's not happening on their own, and what Jim is going to take you through is how SFS or the Stanley Fulfillment System are driving both margins and cash flow, as well as a little more granularity on SG&A. Jim's piece will show you we're building our brand while still maintaining, I think, very good control over discretionary spending and then a closer look into the segments. Don is going to close with a look at some of the market trends that are affecting both our cash flow and our fourth-quarter guidance. So let me turn it over to Jim Loree, our COO.

Jim Loree - *The Stanley Works - COO & EVP*

Thanks, John. We'll stay on the margin chart just for a minute here. And I find this extremely encouraging, considering the 16% volume decline and the 23% reduction in inventories. As John mentioned, we closed out the quarter at 41.3% gross margin. That's an all-time record for the company as he did mention, and the first time in my 10 years that we have been greater than 40%, which is a big milestone. This was done at a time, as I mentioned, when the production volumes are down greater than 30% versus last year.

To expand a little bit on some of the key drivers, the strength of our value propositions has really enabled us to achieve solid price realization, and that's offset a cumulative $440 million of inflation since 2004. The Stanley Fulfillment System is a key to this and transformational lean has been driving productivity in our factories and our supply chain for quite some time. Business mix has also helped as securities become a larger part of the portfolio. And of course the $370 million of cost cuts, a portion of those were in cost of goods sold and have helped enable us to deal with the steep volume declines while protecting our margins.

All this raises the question, the obvious question, is this sustainable? There will be some headwinds going into 2010, as tools and storage mixes up and some of the cost cuts -- probably about 25% or so come back. But it's safe to assume that we're now operating in the neighborhood of 40%, and that's what we expect to record for the year and would I expect you can think of the company as a 40% gross margin company on a prospective basis.

I mentioned the Stanley Fulfillment System. I want to spend a little more time on that. It really involves four components. Let's start with the upper right -- sales and operations planning. This is keeping supply and demand in balance -- so not making too many things when you don't need them. When volume is down, you make less. When volume is up, you make more. We have a phrase we have going -- sell one, replenish one. The idea is to try to make every day what the customers need that day. We're not there yet, but that's the direction we're going in. And I think we have done a pretty good job keeping our inventories in check through a robust sales and operations planning process throughout the company.

Now, we'll move to the lower left -- transformational lean. This is the implementation of lean in all our factories, supply chains, and back offices. Many companies do lean and do this every day. I think the thing that differentiates us is we actually have trademarked our transformational lean phrase, because what we try to do is to instead of incrementalizing improvements, we try to step back and say, how can we change the business model utilizing lean to create a sustainable competitive advantage? We have done that in a few cases, not throughout the company, but that's starting to take effect. And the benefits from lean are felt every day in our productivity performance.

Now moving to the lower right, standardization of processes and platforms across the company to provide us with scalability. That's another important part of the Stanley Fulfillment System. And then finally, the toughest nut to crack but the one we're making some progress on now -- and we have been at it a few years -- is this complexity reduction, or complexity management. This is all about simplifying every aspect of the business to drive profitability and asset efficiency. You can see that manifested in the results.

Now we'll move onto SG&A. SG&A expenses are down 9% versus the prior year, but that doesn't tell the full story, because when you net out the acquisitions, we're really down 14%. You can see the $16 million increase from acquisitions. We've also made $5 million worth of incremental investments in the third quarter, about $20 million annualized. Had a little inflation, some benefit from foreign exchange, and then the actions totaling about $41 million have really enabled us to achieve that minus 14% performance in SG&A.

Despite that reduction in SG&A, the company now is really aggressively building its brand out there globally, but let's start with the USA. It's playoff season. That means our major league baseball presence is at its strongest. Right now we are in three out of the four playoff teams in a very prominent way. We're starting to see some early evidence of increased aided brand awareness in a quantitative sense and we will have much more information on that as we close out the season, and we'll probably share some of that with you at our analyst meeting in November.

The next and newest area is our major thrust into global brand development, and we are sponsoring the English Premier League and International World Cup qualifiers with signage at the base of the perimeter of the field, electronic signage, which comes up and is seen on TV and often seems to be prominent right at the time when goals are scored or people are watching. This is seen by more than 1 billion viewers per week, and interestingly, 40% of the impressions are actually from outside of Europe. You can start to -- when you talk to some of the Asian folks in our company -- you can start to hear the buzz about what their customers are saying about the Stanley brand and the fact they see it on football.

Moving up to the upper left, we're also moving aggressively into social media. Four months ago, we had no presence on Facebook and Twitter. Today we have over 1,000 followers on Facebook and 800 or so on Twitter. Then finally I'm pleased to invite you to surf our just-upgraded IR website at stanleyworks.com. It's a very impressive piece of work.

Now I am going to spend some time on the segments. Security, once again, was the gem of the quarter. Revenues were up marginally, up 3%. Organic growth was down slightly, down 6%. Segment profit was up in double digits and the profit rate exceeded 20%, which was very, very impressive performance. Convergent, the electronic business, revenues were up 13%. Organic was down 5%, but recurring monthly revenue was up 5% organically. The profit rate was up 150 basis points over the prior year. And even though the declines in installations slowed, the national account installations increased and the CapEx constraints, while not completely gone, are starting to loosen.

The big news in mechanical access was the profit rate as well. They did a nice job on price realization and cost reduction actions, et cetera, but the Stanley branded hardware rollout at a major North American retailer is well underway now, will be meaningful from a revenue perspective in the fourth quarter and next year, and the early signs at the point of sale are very encouraging.

Moving on to industrial, the steep revenue declines took their toll on profitability in this segment during the quarter with organic growth down a staggering 30% -- not unexpected, but certainly a difficult story to deal with from a profitability perspective. And their costs in Industrial tend to come out a little bit more slowly than they do in the rest of the company, because this is the most concentrated segment that we have in Europe where the cost takeouts take a little longer to manifest themselves. Segment profit was down 53% to $19 million and the profit rate was right around 9%, which is where it was in the second quarter as well. We believe this is a trough area of segment profit rate for Industrial, and we'll talk a little bit about what we think is happening on a prospective basis in a minute.

The inventory corrections continued to be a headwind. We expect them to continue, perhaps at a slightly lower level into the fourth quarter. And then they should be gone by the first quarter as the Industrial buyers start buying in proportion to their production volume, which is increasing now as we look at the economic statistics.

We've divided the segment into two subsegments for the purposes of describing it to you. It also happens to be the way we manage it at the company. Industrial and automotive repair tools, which is Facom and Proto on the left-hand side, the lower left. Facom was down 27% in revenue, but their new product development remains strong, and the Facom products are also being cross-fertilized in some of the other areas, such as Proto and Mac. I mentioned the European cost reductions and the lagging effect there.

On industrial and automotive supply, which is Mac, Vidmar, and supply and services, the Mac profitability was encouraging. They did have double-digit revenue declines, but they made good progress from a profitability perspective. I think the good news when we step back from the overall segment is that the gross margin and the contribution margin rates are holding up. So we should -- as I said -- be in a trough here and positioned for strong leverage when the volume resumes probably in the first quarter.

Moving onto CDIY -- from my perspective, CDIY was a pleasant surprise this quarter. Volume was still anemic, revenues were down 23%, organic growth down 21%. But the segment profit was down only 11%, and very encouraging was the segment profit rate resumed its expansion and is now hovering around 15%, up 210 basis points over the prior year and also up 210 basis points versus second quarter.

The organic revenue declined. We're seeing some early signs of stabilization, as John alluded to. And I think most encouraging is the Bostitch integration benefits, which yielded significant cost productivity gains in this segment are taking hold. They're ahead of plan. Bostitch profitability is strong and improving, and I think -- knock on wood -- that the long saga of Bostitch related profitability problems may be in the rear-view mirror.

And then finally, the wave of new product introductions that is taking place in this overall segment is going to be significant in the fourth quarter and is expected to accelerate our market share gains, so stay tuned. This strong, strong franchise is going to get even stronger with an array of new exciting products in the fourth quarter, and on top of that, we have the intensifying brand support and brand strength that I talked about earlier. So we're very, very excited about the future here coming out of, hopefully, trough conditions in the marketplace.

And now I'll turn it over to Don Allan, who will take you through more color on the segments.

Don Allan - *The Stanley Works - CFO & VP*

All right, thank you, Jim. Page 16 is a new page we added this quarter, which is a way for us to help communicate some of the key trends in three different segments, both historical, and then some of our thoughts going forward in the short-term.

So if we start with the security segment, which is on the left side of the chart, the top part of the chart gives a historical trend of the segment profit rate, which is the line; and then the bar graphs are the unit volume declines that we have experienced in each segment. So as we dive a little deeper into security and start with the Convergent business, Convergent revenues as you know from installations has been down, but we believe it's likely bottomed out in the second quarter and we also think that attrition peaked in the second quarter as well. We're beginning to experience some stabilization in our order rates in the Convergent business, which is a positive sign.

One thing we've discussed in previous calls is commercial construction in some of the delayed and abandoned projects that we've seen --- that continues to be a headwind. But the good news in that particular story is that it's still more of a delayed situation versus an abandonment of projects. And as long as that continues, that trend, then we believe we will be able to continue to show modest declines and eventually growth in this segment over time.

Focusing on commercial construction as an impact to our company, as many of you know from the end market charts that we provided in the past, it's important to remind you that commercial construction is only 15% of our security segment and only slightly greater than 10% of the total company. So even though we are experiencing a little bit of headwind there, it's important to keep in mind it's not a very significant portion of our total company.

And last but certainly not least, as Jim mentioned in the previous slides, the profit rate accretion in security has been a very good story, considering the declining volume environment we experienced over the last seven quarters where we have gone from a 16% segment profit rate in the first quarter of '08 up to almost 21% in this particular third quarter. And that's really all those actions Jim mentioned around pricing with our customers, cost actions, and then some benefit of deflation and commodities, particularly in our mechanical security business.

Shifting to Industrial in the middle of the page, clearly Industrial improvement in this particular set of businesses is lagging behind, CDIY in particular, and obviously security. As Jim mentioned, we continue to see improvement in Industrial production data, which is showing positive growth and moderating signs. However, our business does lag those indicators and we would expect we would eventually feel that positive impact if that trend continues, likely in early 2010.

The inventory corrections have clearly been significant throughout the year and will likely continue at a modest pace in the fourth quarter of '09. We believe the profit rate has stabilized. But we would expect improvement in that profit rate to be likely in the fourth quarter, as many of the cost actions will be completed in our European operations, and we do believe those inventory corrections will abate.

Last but certainly not least is the CDIY segment. As you can see -- Jim mentioned this, that the operating margin rate or profit rate has gone to 14.8%. So it went from the bottom of 6.4% in the fourth quarter of last year and has really emerged back to very normalized levels for this segment, or very close to normalized levels. But economic conditions continue to be a little tough in this area, although we're starting to see a little bit of positive signs.

In particular, the US housing starts have stabilized. We believe they've bottomed out. Consumer confidence is improving in both the US and the Euro region in comparison to the second quarter of this year. And as a result, you're seeing the impact in our revenues as our revenues are flattening out on a sequential basis when you look at the second and the third quarter. We would expect that trend to likely continue into the fourth quarter. We do expect to experience some modest revenue growth in the beginning of 2010 or the first quarter of 2010 if these trends continue.

Last but certainly not least, that significant profit rate as I mentioned is largely due to the CT&S and Bostitch integration that Jim discussed. So we feel that's a nice summary of our three segments and key trends based on history and some thoughts going forward.

Moving to free cash flow, which was a really nice story this quarter, our third-quarter cash flow exceeded prior-year levels and that was while our continuing ops earnings was actually down from $78 million to $62 million or 21%.

Another item to focus on here is working capital. As John mentioned earlier, a very nice working capital performance where we had a positive working capital benefit and cash flow of $32 million, and we had a 20% unit volume decline in the same quarter.

One item I want to point out here in the other line -- if you look at last year, John had mentioned the sale of CST. There was a gain of $84 million that is being -- that's showing as a negative and other last year, and also the taxes paid on that of about $34 million, which is really driving that. And the total of that is close is $120 million of a negative outflow. So if you remove that, it's a slight positive and it's more in line with the $25 million positive we saw in the third quarter of this year.

CapEx continues to be a good story as we continue to control where we're spending our money and make sure we're spending it efficiently, and we're tracking to that $85 million number for the year and on pace for that. So the end result is free cash flow $158 million versus $103 million last year, which is a 50% improvement year-over-year with earnings being down 21%.

As I mentioned in the last quarter call, we had set a guidance of $300 million of free cash flow for the year and at that point in time, we were at about $25 million of free cash flow year-to-date. Now we're at $183 million, which would be a little more than 60% of that $300 million previous guidance we provided. Based on the work that we're doing in working capital and all the different efforts around SFS, we actually think we can exceed $300 million this year. And that would be consistent with some of our historical trends if you look back. Through three quarters, we tend to be anywhere between 57% or 65% through three quarters in comparison to the annual objective.

Moving to the balance sheet, continues to be a positive story for us. As many of you know, we have been focused on deleveraging our balance sheet this year. Our goal we established was $200 million of a debt reduction or deleveraging goal. We've achieved $161 million of that through three quarters, so we feel like we're tracking very nicely to that objective. And our debt-to-capital ratio is now down to 43%, which is sequentially improved where it was at 46% in the second quarter. And when you adjust it for our equity and debt hybrid instruments, it's now 31% to 33%, which again is an improvement from the second quarter where it was at 34% to 37%. So we feel very good about our deleveraging plan and how we're on track in that regard.

The next page is an update on guidance. As all of you have seen, we have increased our guidance compared to July, so what I'd like to do is just walk through some changes in that guidance. On the left side of the page, our July guidance was a range of EPS $2.34 to $2.84, which was a $0.50 range. What was driving the bulk of that range was the unit volume assumption, which we assumed a negative 18% to a negative 20% at that timeframe for the year. We're starting in this chart with our midpoint to that range, which is $2.59, which clearly is an implied guidance assumption of about a negative 19% unit volume, which is what we're currently estimating for the year. If we take our gross margin rate improvement that John and Jim both talked about earlier, we believe that for the year we will be approximately 40% gross margin. And in July, I indicated that we thought for the second half of the year we would be somewhere between 38% to 39%. So now we believe we will be slightly above 40% in the second half, and it's really being driven by all the things that were articulated earlier around price, productivity, around cost, deflation, et cetera. So we feel positive about that going forward.

The last item is what we call other, which is several different things. Clearly we benefited from FX as the weaker US dollar versus some of the major currencies that are prominent in our world such as the euro and the Great Britain pound. But we also think we could have potentially lower restructuring and slightly lower taxes as well as we close out the year.

I will point out that the restructuring we provided at guidance was about $45 million the previous call. We expect it probably to be somewhere between $40 million and $45 million, so it won't be significantly lower than that number. The end result is a current guidance range of $2.84 to $2.94. If you exclude the gain on the debt extinguishment, that means it's $2.50 to $2.60, which was an increase from the $2.00 and $2.50 that we provided in July.

Moving to free cash flow, as I mentioned earlier, we expect to exceed $300 million in free cash flow, and that's really due primarily to two things, as you can see on the chart here. First, our improved earnings outlook, which is about $0.25 to $0.35 EPS, and then our continued belief that we will able to exceed prior year working capital levels. In the fourth quarter of '08, we achieved 5.9 working capital turns, and we still feel that we will be able to achieve in excess of 6 working capital turns by the end of this year, which is all being driven by the Stanley Fulfillment System and the process controls that we've put in place that Jim articulated earlier in this call.

So in summary, we feel like we're well positioned to continue to gain market share. We've made investments, as you know, around our brand and in some cases advertising. We continue to invest in new product development and increase our direct-to-customer interactions in the security segment in particular to really drive those results. We're seeing modest signs of sequential improvement, which are encouraging, in particular in security and CDIY. Industrial is lagging, but we do believe as 2010 begins that segment will begin to improve.

Gross and operating margins are on track and remain strong for the full year. As Jim mentioned, we do feel that we've established a new line around gross margin where we think we're now a 40% gross margin company. Last but certainly not least, we continue to be dedicated to our ongoing success with SFS, both as a source of cash as well as a competitive advantage.

Kate White - *The Stanley Works - Director of IR*

Sarah, we're ready for questions whenever you are.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Your first question comes from Peter Lisnic. Your line is now open.

Peter Lisnic - *Robert W. Baird & Company, Inc. - Analyst*

Good morning, everyone.

John Lundgren - *The Stanley Works - Chairman & CEO*

Good morning, Pete.

Peter Lisnic - *Robert W. Baird & Company, Inc. - Analyst*

I guess first question on CDIY -- if you look at it in dollar terms, $100 million decline in revenue, and operating income only down $6 million or $7 million. Can you give us some color commentary on exactly how that is occurring in terms of restructuring savings, mix, and price? Because that would seem like things are holding up than I thought they would, given that volume pressure.

John Lundgren - *The Stanley Works - Chairman & CEO*

Yes, Pete. Things are holding up better than you might think in terms of the volume pressure. The biggest driver -- Jim touched on it and didn't get much more granular than we intend to -- the biggest driver is improvement within the Bostitch business. We talked about our intent when we started a massive improvement effort on Stanley Bostitch to take it up maybe 100 basis points a quarter for eight quarters to get it back to double-digit operating margins. We were well on the way a year and a half ago with that program when Bostitch was the business within Stanley hit the hardest by the both industrial and the domestic housing downturn.

We made the decision this time last year to basically combine the CT&S or Consumer Tools & Storage and Bostitch business, which in retrospect was a good decision. We knew it was, not only because we took a lot of cost out, business running separately, that we were running as part of a CT&S business. But it really reinvigorated the product development program, the focus on margins, added some rhythms to a business and both at the customer level and internally. That's had a tremendous impact. We aren't -- we don't intend to get into margin by business, because we found that -- all that by subsegment, all that really does is creates more questions than it raises. But we have Bostitch back to historically, I'll say, high or its line average profitability level. That in and of itself is 70% of the improvement. Jim may want to add a little more granularity to it. Think Bostitch improvement within CDYI, Pete, and that's the big one.

Jim Loree - *The Stanley Works - COO & EVP*

I will just address the other 30% and it is really a combination of all the things I talked about extensively on that gross margin page -- the Stanley Fulfillment System, the transformational lean, the price inflation recovery, and all those elements, as well as there may be some minor mix in CDIY as well with a Bostitch improvement.

John Lundgren - *The Stanley Works - Chairman & CEO*

I'll just follow up so you can get in your follow-up without getting cut off. We've talked about SFS. We've talked about it a lot. Because our Consumer Tools & Storage business was a large, well-managed global business with a global platform, they were 12 months to 18 months ahead of the rest of Stanley in terms of truly implementing SFS, the S1R1 to which Jim referred. And so we've gained more traction quicker in that business, and, of course, the Bostitch business has benefited from that as well.

Peter Lisnic - *Robert W. Baird & Company, Inc. - Analyst*

Okay. That is very helpful. Follow-up question on pricing, again, plus 2 this quarter and plus all year -- how sustainable is that and what piece of that is just related to unrecovered commodity costs that you have incurred in the past versus new products and proactive pricing policies, I guess?

Jim Loree - *The Stanley Works - COO & EVP*

Most of the 2 points is carryover. If you recall, we had a big surge in inflation in the middle of last year. It was in the third quarter of last year that we really aggressively implemented price increases to cover that inflation, and we benefited from those in the fourth quarter of last year and the first three quarters of this year. But we are going to start to see the price realization ebbing back to a more normalized level that may be up 0% to 1%, something like that. And most of that will be in all likelihood in the businesses that incur some sort of commodity inflation, and we have a mixed bag there with different businesses. And as you can imagine with all the commodity fluctuations that go on, if steel goes up, the nail business is affected more dramatically than say the security business. So you can't really predict which segment it might occur in, but we will continue to price to our value proposition and continue to price to recover inflation as and if it occurs.

Operator

Your next question comes from Sam Darkatsh. Your line is now open.

Sam Darkatsh - *Raymond James & Associates - Analyst*

Good morning, gentlemen, how are you?

John Lundgren - *The Stanley Works - Chairman & CEO*

Sam, hello.

Sam Darkatsh - *Raymond James & Associates - Analyst*

A couple of real quick questions. Jim, in your prepared remarks, you mentioned in 2010 a number of the discretionary cost cuts you made in '09 would likely be coming back. Could you help quantify that a little bit? And would that entirely be in the OpEx line?

Jim Loree - *The Stanley Works - COO & EVP*

It would entirely be in the OpEx line, and there was $370 million of total cost improvements that were implemented. And of the $370 million, it's our collective view here that about $100 million or so is likely to come back at some point. Whether they all come back next year or not, we'll see. But there are things like discretionary cuts where we have may have cut travel by -- pick a number -- 40%. Maybe we'll let 20% of that come back because we have the volume to compensate for it.

But that said, we've changed a lot of our practices related to areas. And T&E is a good example where today we have implemented extensively TelePresence, CISCO's TelePresence, and that's providing us a structural cost reduction in T&E. So we don't expect all of the T&E cuts for example to come back. I think there are many other stories like that as we look at the cost cutting.

In addition to that, we've made several structural changes in our various businesses, and John already talked at length about the Bostitch and CT&S integration. That's not coming back. That's a permanent change. We also made some changes in the Industrial businesses where we combined, and you saw the subsets when I was going through the Industrial page -- we combined the management of Facom and Proto, and we combined the management of Mac supply and services and Vidmar, and those changes are not coming back. So we feel comfortable that approximately 25% or so of the cost cuts will come back in successive years. I'm not sure they will all be next year, but that's the way I would think about it.

John Lundgren - *The Stanley Works - Chairman & CEO*

Yes, I think that's good.

Sam Darkatsh - *Raymond James & Associates - Analyst*

Okay. And is where you look at raw materials right now, assuming it's essentially flat on a go-forward basis, what does the 2010 versus 2009 variance look like from a raw materials standpoint?

Jim Loree - *The Stanley Works - COO & EVP*

We're basically -- we've gotten to a stage where we have some pluses and some minuses, but we're not looking at any significant deflation or inflation at this time.

John Lundgren - *The Stanley Works - Chairman & CEO*

And I'll add, Sam, to Jim's point he made during his prepared remarks -- whatever benefit, or I guess it was actually my prepared remarks -- we obviously do this as a collaborative effort. What we benefited this year from raw materials deflation, and you know us well enough that 60% to 70% of our raw materials are steel, then it's nonferrous metals, plastic, resin, et cetera. What we've benefited from we've more than lost in volume absorption or lack thereof. So what is going to affect our margins as much or more than the inflation pricing hedge or arbitrage is where volumes settle out next year relative to this year. I think we've gotten much better at responding quickly to inflationary pressure in terms of our pricing. Jim's words -- and they're the right ones -- were pricing to be paid for our value proposition and where we don't think we have a value proposition to shrink or get out of those businesses as quickly as we can.

Operator

Your next question comes from Nigel Coe. Your line is now open.

Nigel Coe - *Deutsche Bank - Analyst*

Thanks. A couple of quick questions. You talked about the CDIY margins at some length already, but interested to get your perspective. You talked about this being a mid-teen, 16% type of margin business. But given that Bostitch is back on track, you've got some SFS benefits coming through. If you could capture that [8%] volume drop, do you think margins will be more towards the high teens going forward?

John Lundgren - *The Stanley Works - Chairman & CEO*

We're not going to forecast margins by segment. By now you should know that. Your question is a logical one and a fair one. We've just got a lot of history that says forecasting margins by segment and subsegment -- we're never rewarded for it when we get it right or exceed it and we're punished for it when we don't. It's not good for us internally or externally. It's why we have three distinct segments that we think gives us some internal diversification. So your observations are logical, but we're simply not going to go there.

Nigel Coe - *Deutsche Bank - Analyst*

Okay. Then maybe just going a little closer to home -- you talked about the industrial cost savings in 4Q. Can you maybe just quantify those? I'm assuming that that would be sufficient to get you back into double digits for 4Q?

Jim Loree - *The Stanley Works - COO & EVP*

The Industrial -- you're looking for a quantification of the industrial cost savings in the fourth quarter that might be incremental to what was in the third quarter? Is that the question?

John Lundgren - *The Stanley Works - Chairman & CEO*

About the European actions.

Jim Loree - *The Stanley Works - COO & EVP*

Oh, yes. It would be difficult to put an exact number on that, but I would say the cost reductions that we implemented were roughly distributed equivalently across the three segments. Security was a little bit less than CDIY and industrial. So on a proportionate basis, the $370 million was allocated essentially that way. It's fair to say if industrial is -- pick a number -- 25% of the revenues roughly -- then 25% of the $370 million applies to industrial. And you can assume that probably about 10% to 20% of that has yet to be materialized.

John Lundgren - *The Stanley Works - Chairman & CEO*

And Nigel, we know you are not going to get to ask a follow-up, just the way the process works, but just to elaborate a little further -- the other point being 50% of our business in Europe is industrial. So some of the costs will come back, as Jim referred to, but some of the cost actions we have taken, as you understand well, it does take longer to realize the benefits of those cost actions in Europe. So there is as large a benefit, but a meaningful delay in what we're experiencing. That will provide a little bit of an offset to the cost coming back, so we're looking for sequential improvement.

Jim Loree - *The Stanley Works - COO & EVP*

Just to be clear about my math, if we say 25% of $400 million is $100 million and 10% to 20% of that might actually be yet to be realized, we're talking $10 million to $20 million -- that's annualized, so you would have to divide by 4. That's probably roughly ballpark what you could expect there.

Operator

Your next question comes from Eric Bosshard. Your line is now open.

Eric Bosshard - *Cleveland Research Company - Analyst*

Good morning.

John Lundgren - *The Stanley Works - Chairman & CEO*

Eric, good morning.

Eric Bosshard - *Cleveland Research Company - Analyst*

I have two questions. First of all, I understand not projecting margins by segment, but getting to that 20% margin in security -- that was a long, long ago projection, so it's nice to see that number achieved --

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Jim Loree - *The Stanley Works - COO & EVP*

We took a lot of heat for like four or five years, which is why John said what he said.

Eric Bosshard - *Cleveland Research Company - Analyst*

Now you got there, so that is great. The two questions that I have -- first of all, you talked bullishly about the CDIY volumes and that you saw improvement across a number of regions. The US volumes, I think in CDIY, were identical, the year-over-year decline was identical in 3Q as it was in 2Q. You mentioned in your script that you thought actually you could have some growth out of that segment in the first quarter. So I would love to get a little bit more color on what's going on in terms of the improvement there, and should we see improvement in 4Q? And then secondly, can you talk about the cost, incremental cost saves that you should achieve in 2010 from the programs that have been implemented over the last nine months?

Don Allan - *The Stanley Works - CFO & VP*

I'll take that. If we start with the CDIY question, as I mentioned in that particular chart, we're clearly seeing a stabilization effect in that particular business and even some modest improvements. It's really being driven by the two economic factors that I mentioned in the US as well as in Europe. So as we look at the business going forward, we don't expect a dramatic improvement in the fourth quarter around revenue. There could be a slight improvement due to some new product rollouts in that particular quarter, but at this point in time, we're not anticipating that. But in the first quarter, we do expect to see some modest improvement in growth in that particular segment, because we will have, first of all, anniversaried a lot of the significant declines and it's under the presumption that these economic conditions have stabilized around housing starts and consumer confidence in particular and we'll begin to see very modest growth rates there.

The second question was around cost carryover effect, I believe, in which as Jim mentioned, we do have about $100 million of cost carryover into next year. So we had $370 million of costs that were executed on, $265 million are 2009 benefit, and about $100 million or more rolls over to 2010. The real question is how much of that will be sustained. Jim gave a lot of feedback on that.

Over time -- he was referring more to the long-term -- 25% of that will probably creep back into the system. That does not mean in 2010 that $100 million of costs will creep back into the system to offset the complete carryover effect that we expect to experience. My estimate would probably be for 2010 that we would be able to maintain anywhere from 50% to 75% of that carryover in 2010.

Kate White - *The Stanley Works - Director of IR*

Sarah, we can move to the next person.

Operator

Your next question comes from Ken Zener. Your line is now open.

Ken Zener - *Macquarie Research Equities - Analyst*

Good morning.

John Lundgren - *The Stanley Works - Chairman & CEO*

Hey, Ken.

Ken Zener - *Macquarie Research Equities - Analyst*

I was wondering if you could comment on security integration in regards to maintaining your growing share and how that relates to the people you have acquired -- so your feet-on-the-street approach -- versus your market share enhancement, and if that really did impact the national versus smaller accounts.

John Lundgren - *The Stanley Works - Chairman & CEO*

I think I understand your question, Ken. Let's start with -- we've made one midsized acquisition in the last two years, and it's going extraordinarily well. We, at this stage, would regard Sonitrol and HSM as fully integrated, and functioning as a very cohesive unit under Brett Bontrager's and Tony [Varley]'s direction, producing nice margins, doing a good job on national accounts. As you know, we have a very strong position in retail. Retailers in general are under a lot of pressure so when a retailer goes out of business, the objective is to get more than our fair share of re-signs, which we are doing and doing a pretty good job at. So we're maintaining or gaining share with national accounts and Tony's team is a doing a real nice job with some of the smaller businesses, rolling them up and gaining share at the local level.

In Europe, the GDP acquisition hasn't had a full-year anniversary yet. I can say that's going very well at the same time. As we mentioned on previous calls, our security business in Europe was relatively small. It was UK centric. We've inherited an extraordinarily capable management team with GDP, a management team that was interested in carrying on with Stanley, and they've done a very, very nice job leveraging their strong market position and gaining share primarily in France and Belgium, where they're a strong number two in the marketplace as well as expanding across borders. I hope that gets at the question you were asking.

Ken Zener - *Macquarie Research Equities - Analyst*

It does. And then could talk about the contribution from the load in or sales that you expect as the hardware reloads and how that can impact 2010 organic?

John Lundgren - *The Stanley Works - Chairman & CEO*

Sure. We're happy to do that. Go ahead, Jim.

Jim Loree - *The Stanley Works - COO & EVP*

Ken, you may not recall -- because I don't think you were following us at the time but in the -- maybe you were -- February '07 analysts' meeting, we talked extensively about the loss of a major customer in the hardware business, which actually cost us over $50 million of lost revenue. And we indicated at the time that we would pursue other customers because we really believe in the strong brand pull and product end user demand for Stanley hardware in the marketplace. And so we indicated at the time we thought -- because for various reasons we weren't going to recover any time soon with the customer we lost the business with that we would pursue other customers and in fact committed at the time to replace at least 50% of the lost revenue over the coming years. And as it turns out, I think this program we're implementing right now, which is about 300 stores into it and has 1,400 to go, next year should have an impact -- annualized it should have an impact of greater than $30 million and next year probably three-quarters of that.

John Lundgren - *The Stanley Works - Chairman & CEO*

So simply said, we have replaced more than 60% of the lost business, and we think in due course we will have replaced it all, but it's going to take another year or so to get us there.

Operator

Your last question comes from Michael Rehaut. Your line is now open.

John Lundgren - *The Stanley Works - Chairman & CEO*

Mike, do you have a question?

Michael Rehaut - *JPMorgan Chase & Co. - Analyst*

Yes, can you hear me?

John Lundgren - *The Stanley Works - Chairman & CEO*

Yes, we can now. You may have been on mute. We didn't hear you before.

Michael Rehaut - *JPMorgan Chase & Co. - Analyst*

The first question, just -- and I know you don't get into forecasting by segment, but more just trying to get a sense of timing, if you will. When you look at the CDIY improvement, and certainly a good portion of that from Bostitch but also from your productivity in SFS, et cetera. I would assume obviously you're doing a lot in the industrial segment as you have been mentioning as well. Can you give us a sense of timing in terms of perhaps when you might expect those cost saves? You mentioned you would expect them to start to bear fruit in 4Q, but are we looking at a 12-month or 24-month type of improvement or maybe even shorter than 12 months given the solid improvement we have seen in CDIY?

Don Allan - *The Stanley Works - CFO & VP*

Mike, this is Don. I will be happy to answer that question. As I mentioned a few minutes ago, our cost programs have been fully executed, except for the European actions and some small actions in our CT&S and Bostitch integration. We would expect by the end of this year, 2009, that all the European actions will be complete and behind us. And Jim mentioned that on an annualized basis, those actions in Europe probably add up to about $20 million to $25 million on an annualized basis. So by the end of the year, those cost actions will be complete and behind us. And what I was referring to earlier for 2010, around $100 million of carryover. That would be the carryover cost of all actions we completed this year and that specifically was what I referred to.

Michael Rehaut - *JPMorgan Chase & Co. - Analyst*

Okay. And just the second question on the new product rollout that you have mentioned, earlier in the presentation you talked about how it's -- you believe it's going to be a very positive impact, market share gains, et cetera, a wave of new products. I think I heard towards the end of the presentation -- perhaps, Don, you had been talking about more of a slight improvement from new product rollouts. So I'm just trying to maybe reconcile those two comments and trying to get a sense of what actually you're expecting in terms of a contribution to sales growth.

John Lundgren - *The Stanley Works - Chairman & CEO*

Mike, this is John. I guess two things. As you know -- because you have followed us a long time -- we have a tried, tested, and proven steadfast etched-in-stone rule. We don't talk about or show a new product to the investment community until our customers have seen it. That has served us well over time. And that won't change.

You have been invited to and hope you can make our -- we think very comprehensive analyst meeting on November 17 in New York where our business heads, specifically Jeff Ansell, Brett Bontrager, Justin Boswell, and Jim and three of his leaders in the industrial segment will be talking about all their products. Then you will actually be able to see them because we will have presented them to the customers.

We intend to have a vitality index that stays above 25%, and the reason I couldn't answer your question, even if I wanted to -- that's what's new; how much of it is incremental. We were very pleasantly surprised when we introduced FatMax Extreme, as a good example, going back a year or two, that far less of the Extreme volume cannibalized FatMax, so in fact that was a much bigger lift on a net basis than we had anticipated. We have no way to predict that at this stage, so I couldn't answer your question if I wanted to, other than historically, we have had as much as $70 million on an annual basis of revenue growth from new products. The question is that's never 100% incremental. It's how much of it is cannibalized, and it remains to be seen.

Operator

There are no further questions at this time. We now turn the call over to you, Ms. White.

Kate White - *The Stanley Works - Director of IR*

I want to thank everybody for participating in our call and our webcast today. As I said at the beginning of the call, if you have any questions or need further information, please feel free to reach out to me.

Operator

This concludes today's conference call. You may now disconnect.
