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SWK - Q4 2012 Stanley Black & Decker, Inc. Earnings Conference Call

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OVERVIEW:

Management discussed 4Q12 results, reporting GAAP EPS of \$0.79 on revenues of \$2.7b. Guidance was for 2013 diluted EPS of \$5.40-5.65.



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PRESENTATION

Operator

Welcome to the Q4 and full-year 2012 Stanley Black & Decker, Inc. earnings conference call. My name is Lorraine and I will be your operator for today's call. At this time all participants are in listen-only mode. Later we will conduct a question-and-answer session. Please note that this conference is being recorded. I will now turn the call over to Vice President of Investor and Government Relations, Kate Vanek. Ms. Vanek, you may begin.

Kate Vanek - *Stanley Black & Decker, Inc. - VP, IR & Government Relations*

Thanks, Lorraine; good morning, everybody. Thank you so much for joining us for the Stanley Black & Decker fourth-quarter and full-year 2012 conference call. On the call in addition to myself is John Lundgren, CEO; Jim Loree, President and COO; and Don Allan, Senior Vice President and CFO.

Our earnings release, which was issued this morning, and a supplemental presentation which we will refer to during the call are available on the IR portion of our website, as well as our newly revamped iPhone and iPad app and mobile website. A replay of the call will begin today at 2 p.m.; the replay number and access code are in our release.

This morning John, Jim and Don will review Stanley's 2012 fourth-quarter and full-year results and various other topical matters followed by a Q&A session. Because of the size of the Q we will be sticking to be one question per caller. As always, please feel free to contact me with any sort of follow-up questions.

And as I normally have to do, we will be making some forward-looking statements during this call. Such statements are based on assumptions of future events that may or may not prove to be accurate and as such they involve risk and uncertainty. It is therefore possible that actual results may differ materially from any forward-looking statements that we might make today.



We direct you to the cautionary statements in the 8-K that we filed with our press release and in our most recent '34 Act. With that I will now turn our call over to our CEO, John Lundgren.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Thanks, Kate; good morning, everybody. This morning, beyond reporters reporting our fourth-quarter 2012 results and providing 2013 guidance, which I know everyone on the call is interested in, a couple other objectives to this morning's call are to essentially close the books on the Black & Decker merger and, of equal or even greater importance, lay the groundwork for what we believe is a series of really exciting organic growth initiatives. So thanks for joining us early this morning.

Quickly on the fourth quarter, revenues were up 4% to \$2.7 billion, half of that was organic growth up 2%. Very interesting on the organic growth -- 6% in CDIY and Engineered Fastening, two of our strategic businesses performing really well and those -- that growth was offset by declines in Europe due primarily to market conditions in IAR as well as Security. A little more on that later.

Diluted EPS of \$1.37, combination of strong operations and a favorable tax rate. That was up 12% versus same period year ago. GAAP earnings were \$0.79. Full year revenues up 8%, 2% organically and 2012 EPS of \$4.67 ex charges was flat versus prior year. But if you normalize the tax rate, i.e. equal 2012, make it equal to 2011, diluted EPS GAAP was \$2.70. But with a normalized tax rate would have been a 12% increase year on year.

And Don is going to provide a lot more granularity on tax and its progression, 2011, 2012 to 2013, when he gives you some more detail on the outlook.

Strong year in cash flow, \$1.1 billion ex charges for the year. Working capital turns of 7.5, a 42% increase since the pro forma pre-merger levels. 2013 guidance for diluted earnings of \$5.40 to \$5.65 a share, that is a 16% to 21% increase versus 2012, driven by organic growth in the range of 2% to 3%, 100 basis points of which we believe will be driven by the early returns on some of the organic growth initiatives that Jim is going to walk you through a little later on this morning.

And finally, March 2013 marks the three-year anniversary of the merger between Stanley and Black & Decker. It's an important milestone; it came with a few notable executive management changes and those were announced in a press release on January 14 and they are taking effect during the first quarter of this year.

So let's turn to the final chapter of the merger. And I guess it's both a pleasure and my good fortune to be able to talk about it, at least on this call, this morning and it's probably the last time we will talk about it in any particular detail. But let's wrap it up.

We did really well on cost synergies. By the end of 2013 we will have achieved \$500 million in cost synergies, significantly exceeding our target and commitment of \$350 million. We exceeded that target by 43%.

Now as you all know, CDIY right now represents about 50% of our revenue. The \$760 million in CDIY of operating margin in 2012 exceeded the entire 2009 operating margin of the entire Company, legacy Stanley and legacy Black & Decker combined.

That's the impact of cost and revenue synergies, of prolific new product development activity in process and exceptionally strong execution by the CDIY team led by Jeff Ansell and comprised of really the best athletes from each of the two legacy organizations. So it was just a terrific opportunity and thankfully, in retrospect, we were able to take advantage of it.

Revenue synergy projects continue to yield strong results. We surpassed \$300 million in revenue synergies versus the goal of \$300 million to \$400 million. And probably the simple example, just to refresh everyone's memory, Stanley Hand Tools are up \$25 million in Latin America or will be by the end of 2013. Business was virtually nonexistent as we were able to sell our premium branded Stanley products through a well-established Black & Decker distribution network, it's just one of many, many examples of the power of the combination of these two companies.

The cultures, driven by world-class innovation, have resulted in more than 1,500 new products and \$1 billion of organic growth over the last three years. And probably one of the greatest achievements in terms of results from the combination is the degree to which the Stanley fulfillment system has been initially embraced and fully embedded across the two companies.

Working capital turns were 7.5 up from 5.3 pro forma pre-merger levels. And within the CDiy, which is where the majority of the integration activity went on, working capital is down 50% from the 2009 pre-merger level. That is a lot of freed up cash to reinvest in our business. So by all measures we truly believe the merger to date has been a resounding success.

Let's move on to the quarter. In terms of sources of growth, as you saw in our earnings release this morning, Stanley grew 4% in the fourth quarter, 8% for the year. Of the 4% in the fourth quarter, it was 2% organic which was 2% volume and flat on price, acquisitions added 3%, currency was a 100 basis point headwind for a total of 4%.

Quite similar to how it played out for the year where volume was up 2%, price was flat leading to 2% organic growth, acquisitions added 8%, currency was a 200 basis point headwind and that yields the 8% total growth.

Looking quickly by business, to give everyone a flavor for the fourth quarter and the year, exceptional performance with our Professional Power Tools in the quarter and on the year driven by the 18 and 20 volt lithium-ion DeWALT product introductions -- just tremendously well accepted across our customer base.

The Consumer Products Group also had a terrific fourth quarter and a great year. The fourth-quarter 9% was driven primarily by new products, Gyro and Matrix as well as some really good acceptance of some of the -- of the smaller products in Japan, which is a small but important market where that business continues to perform well.

Engineered Fastening another bright spot, up 6% for the quarter, 9% for the year. MAS Commercial up 3% for the quarter reversing a trend where they were down on a year-to-date basis. Hand Tools & Fastening was flat for the quarter, 2% for the year. Europe actually grew, but offset by the US where we made the conscious decision to exit some lower margin businesses in Hand Tools & Fasteners.

Infrastructure down 2% in the quarter, 6% for the year. The primary driver there was our oil and gas business where the Onshore business was slow across the board, offset partially by strong growth, albeit from a low base, in the Offshore business. And Jim is going to talk about that a little bit in his section a little later on.

Quickly, Convergent Security was off 3% for the quarter and for the year. US Security actually grew in the fourth quarter; most of the decline of was Europe and a lot of that was Niscayah, much of which was planned.

And finally, last but certainly not least, IAR was down 5% for the quarter, 2% for the year. You will recall that IAR is one of our few businesses where we have more business in Europe than the US due to the extremely important Facom franchise among others.

That franchise is stronger than ever. I won't dwell on European market conditions, but we have at a minimum maintained and likely gained share in Europe by being off only 2% for the year in our Industrial & Automotive Repair business.

So key organic growth initiatives are in process, we're going to expand on this and put a couple of programs in place to rev up the engine for a couple of our smaller businesses that are lagging fleet average in terms of performance.

Let's look real quickly on a geographic basis; I don't want to spend too much time on this. But upper left, if we want to look at North America, a very strong quarter in Canada and a very good year. More importantly, the US, which accounts for 48% to 49% of our business, grew 1% in the quarter, 1% for the year. CDiy and Security were up, offset by the Industrial segment, as we talked about, on an ongoing basis.



Moving to the middle of the chart, Europe was off 3% in the quarter, 2% for the year. It does represent 26% of our business. Again, in the fourth quarter CDIY grew while Convergent Security, primarily Niscayah as well as IAR, were off in the fourth quarter. So a total of 3% organic volume decline, 2% for the year. Emerging markets remain -- go from strength to strength, a plus 15% quarter, 11% for the year.

And then just very, very quickly, Japan and Australia together account for 4% of our business. Japan a flat quarter but very strong year driven by Engineered Fastening. And Australia was down high-single-digits. We think we have a program in place to leverage the opportunity to improve collaboration between IAR, CDIY as well as leverage the infrastructure of backroom capabilities with Stanley Security Solutions.

Let me turn it over to Jim who is going to spend a little less time than normal on segment detail. And we have included a great amount of detail in the appendix so he can spend a little more time on introducing some of the growth of initiatives to which I have spoken.

Jim Loree - Stanley Black & Decker, Inc. - EVP & COO

Okay, thanks, John. As John indicated, I will hit the segment info fairly quickly. It is a fairly clear and relatively simple story this quarter operationally. And the first part of the story relating to CDIY is just a terrific performance by that team with 6% organic growth and 180 basis points of profit rate accretion. The organic growth was 7% in North America, we had double-digit growth in the emerging markets and we were flat in Europe.

Now of all those accomplishments I would say the last one perhaps was the most challenging to deal with and perhaps the most impressive, because they were able to take what in Southern Europe was a down 10% to 20% type of performance across those countries and translate it into an overall flat performance, really outstanding work in the UK and real strong in other parts of Europe excluding the South as well.

So they've taken the new products and they have done some really creative promotions and they have really worked hard to offset the difficult market conditions in Europe.

Now moving to the global business, the Professional Power Tools up of 14%, as John mentioned, Consumer up 9%. Hand Tools & Fastening was flat as new storage products and Black & Decker Hand Tools strength were offset by lower US sales as we exited some dilutive margin promotion activity that we had engaged in last year.

What's really impressive to me is the profit rate, 14.5% in the fourth quarter, that is really strong for the fourth quarter for this type of business. And as you probably recall, the margin rates have been pretty strong in CDIY all year.

And we think that as we enter 2013 with strong organic growth momentum that we have a new watermark for operating margin right that represents a sustainable, at least we think sustainable level with perhaps room for even further improvement -- in a home market that is firming up as we sit here today and a solid new product pipeline, so we are pretty bullish on this segment for the future.

And then moving to Security and Industrial, the story is -- it was articulated as basically weakness in Europe and both these businesses negatively impacted the growth and profitability in the segments. Security had negative 3% organic growth and positive growth, albeit 1%, but still a sea change in terms of performance in CSS North America and we are happy to see that -- minus 5% in Europe and the Mechanical Access business, which is primarily US, was up 3%.

The operating margin rate in Security was 15.5%, essentially flat, down 20 basis points versus the prior year and 17.3% excluding the Niscayah dilution or rate dilution that occurs because of the lower rate. Although the Niscayah integration is continuing to progress smoothly and they've essentially doubled their operating margin rate since the inception of that integration activity.

CSS overall was down 3% organically, North America up 1% and minus 5% in Europe. And as I mentioned, the Commercial Hardware organic sales were up in total 3% and in North America 4%.

We have a very interesting business model shift going on in Mechanical Access in the US and that is that we're converting our direct business to be served by independent distributors, which is freeing up our sales force from the transactional activity to become much more hunters -- hunter



type activity. And also, this change enables us to really pursue more aggressively the Commercial Construction market which is heating up as we speak.

So that is the story for Security. Industrial 16% operating margin rate, down 40 basis points versus the prior year. The operating leverage in Engineered Fastening, continuing great performance there offset by the declines in IAR Europe. And John talked about the numbers with IAR down 5% organically, Engineered Fastening up 6% and Infrastructure down 2% for a total of negative 1% organic growth.

Engineered Fastening at 6% positive was a really good story when you put it in the context of the light vehicle production globally which contracted 1.5%. And they also had a terrific performance in Europe being up 3% despite the issues on that continent. And they also, the team at Emhart also made terrific progress planning for the Infastech integration which we expect the deal to close here over the next several weeks. So all that very encouraging.

The Infrastructure business, the declines moderated, so trend is getting better there. And actually Oil & Gas, the larger part of the segment there or the sub segment, was slightly positive organically, reflecting what we think is a bottom in the US Onshore market which is very encouraging.

In fact, we see activity beginning to become -- pipeline activity beginning to generate very significant activity in North America. And then Offshore remains strong. The issue that made the sub segment negative was the hydraulics business was down about 10% relying heavily on -- end market relying heavily on scrap steel, which was a tough story in the latter half of the year.

So that is the segment information for this quarter. Now I would like to spend some time on the initiative that we as a team have been aggressively pursuing for about six months now. And we think the number one catalyst for positive revaluation of the Company in the stock market will be the demonstrated capacity of this team to achieve 4% to 6% organic growth, which has been a long-standing objective of ours ever since John's arrival.

And if you average out the organic growth over the long term, we've been running around 3% if you exclude 2009, which was kind of an outlier of a year. It would be about 1% if you included 2009. So we haven't really hit that objective and if you look at the last five years there are lots of external factors that have been attributable to that.

However, we cannot accept the fact that the external environment, A, has been weak and we cannot accept the lower performance just because the external environment has been weak. And we don't really expect the external environment to be much better over the next five years with continued issues in Europe, slow growth in the US and maybe somewhat slower but still robust growth in the emerging markets.

So as a team we decided that we would take matters into our own hands and we would rev up our organic growth engine. And a lot of the acquisition activity that we pursued over the last few years has put us in a position where we're actually able to do that, leveraging some of the value propositions that we have acquired and capabilities that we have acquired over the years.

So we have an initiative, I've talked about it before, which adds up internally to slightly over \$1 billion of revenue over a three-year period. We are going to commit to \$850 million which will give us the ability to tack on a couple of points of organic growth on top of the 1 to 2 to 3 that we kind of expect attributable to all our other activities in our core activities in these relatively slow markets.

So that is how we are going to get to 4% to 6%, we're going to have these incremental activities that require some significant funding and a lot of execution. So about \$100 million of operating expense investment over the three-year period with about \$65 million of it this year and about \$50 million of one-time CapEx is the price for implementing these programs.

I'm going to talk about emerging markets, which is the single largest element of the \$850 million -- \$350 million. But first let me just quickly cover some of the other ones that add up to the other part of this major initiative.

Very exciting is the Smart Tools & Storage element. It's about \$100 million, includes MRO vending, tool locating systems, electronic (inaudible), it leverages our CribMaster and AeroScout acquisitions and we are in the process now of adding about 40 sales executives, primarily in the US, but also in some other areas around the world. That is underway and looking very, very positive.

\$150 million will come from healthcare and security verticals. The acquisition of Niscayah and AeroScout enable us to take a whole new approach to healthcare where we can bring safety, security, efficiency and compliance to hospitals at a time when they sorely need it and in many cases are desperate for improvements in these areas just for the health of their enterprises.

And we have a value proposition which is very, very powerful and we have really developed it at this point in time. And now it is incumbent upon us to take it to the market and start selling it. And so, we are adding about 75 account executives in healthcare and education, which is also obviously in the security vertical -- a very, very relevant place to be right now. And the hiring of these folks as well underway, the value propositions are intact and I'm very confident we will get to the \$150 million.

Then on the US government, you might ask why go into the US government right now when the spending looks like it is going to go down about somewhere in the neighborhood of 5% to 10%. But the reality is as the -- as we look back in our market share with the US government over time we're kind of underweight in this area and we haven't attacked it in a very efficient manner over the years.

And so, what we are finding is that we need to have feet on the street at the locations where things are actually purchased by the government and not necessarily just in Washington. So we are putting about 20 people on the street to cover US government in the regional areas with focus on California, the South and Virginia and we expect the US government sales to increase by about \$100 million over a three-year period. And that will cover several of our different businesses including CDII, IAR, the Security business and healthcare.

And then we have Offshore. Offshore today has already been a great story, somewhat masked by the weakness in Onshore which, as I mentioned, is now subsiding. And Offshore is going to continue to grow, it is about \$100 million today, it was about \$20 million when we bought CRC.

And the latest chapter in that exciting story will have to do with two things and primary things. One is building portable spool bases, which is kind of a revolutionary idea that our CRC folks came up with which helps the pipeline companies save enormous amounts of money by moving the spool bases to where the oil is as opposed to just the fixed spool bases that exist today.

And then the other area is a major push into Malaysia where the offshore activity has increased dramatically over the last few years and we are in discussions now with the major producers, pipeline companies in that area to implement a major growth program there.

And then the final part of this is just finishing up the Black & Decker revenue synergies. As John mentioned, we are closing the book on the merger today, so we won't be talking about that much more. But we didn't want to lose sight of the last \$50 million of revenue synergies that we have planned for that. And so we will just track it and manage it using the process that we are using here to drive this organic growth engine.

And that process is basically taking the integration approach that we used so successfully over the years from our various acquisitions and using that kind of program management, resource allocation, tracking, monitoring, pulsing type of an approach to ensure that we manage this organic growth initiative as tightly as we did those various acquisition integrations. And that is underway and so far so good.

We feel real confident that we know what the status of the one of these initiatives is, and that if we do run into issues that we will know quickly and be able to respond quickly. So all of these initiatives are up and running, we will generate a minimum of \$100 million of organic growth as a result of them in 2012, and then another \$350 million to \$400 million a year for the following two years after that.

And the thought is that once we get through this that we will have made enormous progress -- just like we did with the Stanley fulfillment system -- in making this organic growth part of the fabric of the Company and therefore changing the inherent structural organic growth rate of the Company up into that 4% to 6% range which we think will have enormous value creation potential for the equity.

So let's move on to a little bit more color on what we are doing in the emerging markets. And this is really a major step function change in the way that we are approaching emerging markets. Historically we have managed the various regions of the world as tight P&Ls with incremental investments generally made at the local level, monitored by the businesses with input from the businesses.



But because of the tight P&L management, and most of these initiatives when you make the investments the payback is greater than one year. So any time that there were external market issues or that type of thing there was frequently kind of pulling back on the incremental investment. And we still, despite the fact that we only made incremental investment we still had terrific growth from the emerging markets.

And today they represent about 15% of the Company. They typically have grown over the last five years about 20%; last year was slightly lower than that as they have slowed down a little. But they continue to be major growth drivers, they continue to have above line average operating margins, so roughly in the neighborhood of 20%. It will -- the operating margin will go down slightly as we make some major funding commitments, but it will still be well above Company line average.

So we have funded a major push. As I mentioned, the total that we're spending this year will be about \$65 million and a good half of that, slightly more than half of that will be spent on the emerging markets where we are going to add about 1,000 commercial resources over the next three years and that, as I said, is well underway.

We are also moving the management of these various markets from a business led center of gravity with, generally speaking, US headquarters to a regional led center of gravity -- led by one individual who was appointed in the fourth quarter, Jaime Ramirez, who ran our Latin American business for -- first with Black & Decker and then with Stanley Black & Decker and grew it from \$200 million to about \$900 million over an eight-year period.

He is a proven veteran who has aggressive growth, a track record and also strong profitability management and people management. So he is the right guy, he is on board, he's about four months into -- excuse me, three months into his planning process, he's got his organization assembled and we are off and running.

We are also moving from high price point Western design products, which only cover about 10% to 20% of the market, to mid-price point products which will be designed locally which address about 70% of the market.

Now the high price point products will continue to sell because over time we would like to move our MPP customers up into the high price point products. But the heartland of the market right now in the emerging markets is the MPP. And these products need to be designed locally by local engineers who are in touch with local market customs and local market needs.

So we have formed three new SBUs with global emerging markets responsibility because one thing we have found is that, although there are nuances from region to region, many of the products across all these markets are very, very similar. And so with late point identification we can have a relatively streamlined product structure. And those three SBUs are in power tools, hand tools and commercial hardware.

And then the other thing that we're going to do is we're going to go from a limited MPP line, which we talked about, much of which is sourced, and we are going to go to much more of an in-house manufactured line in the emerging markets and for the emerging markets with local plants that are dedicated to local markets.

We can't have high cost plants that serve the West, even though they are located in the emerging markets, serve the local markets because we can't get to the right cost structure. So we will have several new plants; we started that with the opening of an Indian plant last year and we will have plants in China and Turkey, we will expand our plant in Brazil and we will continue to build plants as necessary as the volume begins to build up.

This will not require enormous capital expenditures. There will be a combination of small acquisitions and relatively small capital expenditures for these plants. We're also moving from an under-resourced commercial organization in the emerging markets to a very significant troop movement with feet on the street sized to the market opportunity and over 1,000 commercial resources to be added.

And you might say, well what does that mean in the context of what you have now? And it will be more than doubling the resources that we have in those markets today, so just to give you some context.

And then finally, we are going from separate CDiy and IAR efforts in Tools & Storage to one unified effort focused on growth. Now as a company we are the only one with power tools and hand tools. We are also the only tool company with strength in both the CDiy and the IAR channels. And it is very interesting when you get into these markets the channels become very blurred between CDiy and IAR.

So instead of spending a lot of time trying to figure how to take our structure and account for it and manage it in a way that isn't a natural fit with the markets, we are going to leverage the advantages that we have, the power tools, the hand tools, the CDiy, the IAR.

And we have constructed an internal JV which will take the best elements of CDiy's aspects and IAR's and it will be managed by the leader of the region. And there will be no time wasted on internal things like trying to sort out who gets credit for what. It will simply be focused on growing in the marketplace, which will help us drive these powerful results.

So this is a pivotal moment in our Company's evolution in my view. I think in the past we've demonstrated prowess and cost control, acquisition integration, deal execution, working capital management and so on. But as I mentioned earlier, our organic growth has been okay but not superior, not an out-performance, let's say, for what it could be.

That is despite the fact that we have more than quadrupled the size of the Company over the last 10 years and now we are going to add organic growth to the fabric of our culture and I think it will be a very, very positive thing for our employees and our stockholders. I will turn it over to Don now for the rest of the financial presentation.

Don Allan - Stanley Black & Decker, Inc. - SVP & CFO

Thank you, Jim. So I would like to start with a review of free cash flow on page 13. As you can see, our free cash flow performance was very strong in 2012. One thing I would like to highlight though is this financial statement is a little different than what you have seen in the P&L which excludes HHI.

The cash flow statement actually has the impact of HHI in it for the majority of the year. However, it does not reflect a full year cash flow performance for HHI because we did close that transaction in early to mid December. And as a result there's roughly \$30 million of lost free cash flow associated with HHI. So when you adjust for that our performance was about \$1.1 billion and compared to the \$1.060 billion that you see here on the page.

One thing I would like to point out as well is that our working capital performance, as John mentioned, was very, very strong, up to 7.5 from 7.2 in the prior year which generated in the fourth quarter almost \$350 million of free cash flow. It was slightly short of our expectation, we expected it to be slightly above \$400 million of free cash flow in the fourth quarter, as I mentioned back in October.

And that is really the gap that you see, the \$1.1 billion versus our guidance of \$1.2 billion. That's all set aside, a fantastic performance of free cash flow overall, two years in a row, in excess of \$1 billion and it continues to be a strong part of the story for our Company.

A couple items of note as well here on this page, there was a large gain associated with HHI that is included here that we are actually backing that out. So it is included in net income and then it is backed out so it doesn't affect the operating cash flow.

A very tax efficient transaction selling HHI, which I think most of you are aware of. The gross -- the pre-tax gain was almost \$390 million and the tax effect -- or effective tax rate was \$25 million. So a very nice story there with less than 10% tax paid on the gain associated with that transaction.

And then the last item to mention would be our CapEx. CapEx was relatively in line, about 2.5% of our revenue for the year, and we would expect that going into 2013 we would see a similar trend or percentage of revenue as well.

So the last take away on free cash flow is that we feel this is definitely a differentiator for our Company; we'll continue to focus on working capital improvements going forward. As you know, we have a road to get to 10 working capital turns and we still feel there are many areas of improvement that are available in our businesses.



So with that I would like to move to 2013 outlook. For EPS we expect to be between \$5.40 and \$5.65 for the year, which would be a 16% to 21% EPS growth versus 2012. Let me walk you through some of the assumptions associated with that. First organic growth. Organic growth we expect to be up 2% to 3% which would be an accretive impact on EPS of anywhere from zero to \$0.15.

Breaking that down into a little more detail, the core businesses we would expect to grow somewhere between 1% to 2%, so relatively consistent with the performance that we saw in 2012, which adds accretion of \$0.15 to \$0.30 EPS.

As Jim touched on briefly, the organic growth initiatives will yield about 1 point of revenue in 2013; however, they will be slightly dilutive to EPS, \$0.15 specifically, as we will make investments to ensure that we can achieve \$850 million of revenue in three years and \$200 million of operating margin in that same time frame.

It's more of a timing issue and it's something just to be cognizant as we make these investments and ensure that we are successful over the next three years of this growth initiative.

The next area would be cost synergies associated with our two larger acquisitions, BDK and Niscayah. As we close the book on BDK we do still have some revenue synergies that Jim touched on to execute on in 2013 as well as \$50 million of cost synergies.

That would have a cumulative effect of \$500 million of BDK cost synergies and really close the book on that transaction; \$35 million of Niscayah synergies, which is year two, and we continue to progress forward with really trying to achieve an OM rate above line average for Niscayah within our Security segment; \$0.20 EPS accretion associated with Infastech, so it is slightly better than the \$0.15 that we provided three months ago.

The transaction is not closed at this point; we do expect that it likely will close hopefully before February 1. But if for some reason that doesn't happen due to the regulatory approval process in China specifically, then we'll provide an update accordingly as needed.

Carryover effect of our cost actions from 2012 we expect to be \$0.15, which is slightly lower than our October view as we have allowed some customer facing headcount and T&E adds to come back into the system to make sure that we drive organic growth.

The next area is associated with the share repurchase. So as you know, a large part of the funds with the HHI divestiture were going to be utilized to repurchase shares. We entered into an accelerated share repurchase program in early December that was executed on post the closing of HHI.

As a result approximately 80% of the \$850 million share repurchase, which is up from the \$700 million we originally communicated, was executed on in late December. And as a result 9.3 million shares were retired associated with that at a cost that is in the low [\$70 millions] from a stock price perspective.

The remainder of the 20% of the \$850 million will be executed on in the second quarter where the total EPS impact will be a positive \$0.37 for 2013 resulting in an average shares outstanding, as you can see, of 155.9 million.

Then we have several other areas that net to a neutral impact that we've touched on before such as FX, price and inflation, the negative mix carryover effect that we experienced in 2012 and then some positive impacts from some smaller acquisitions such as Powers, AeroScout, et cetera. All that will be net neutral to 2013.

The next area is tax, and I would like to clarify a few things in tax especially related to 2012 before I walk through the guidance. Our tax rate in 2012 for the year was 19.8%, that is on a continued operations basis. If you include HHI in our results for the year the tax rate would have been 22%, which is right in line with our guidance of 22% to 23% that we provided in January and reinforced throughout the year as well as in October. The Q4 associated rate with that 22% was 17%, again in line with our expectations.

So I just want to make sure I clarify that because there were a few questions early this morning related to the tax rate in 2012, which was in line with our guidance expectations.

So what does that mean going into 2013? Well, we do expect our tax rate to increase in 2013 to 23% to 24%, which does create a headwind in EPS, as you can see, of \$0.20 to \$0.30. Why is that? Well, in the last two years we've had some significant tax audit settlements. In 2011 those settlements were over \$100 million, \$105 million specifically. And in 2012 they were approximately \$42 million.

When you adjust the effect of those one-time items the tax rate is between 23% and 24% for those years, which is really the new base for us going forward. We've settled a lot of the old years associated with tax audits and we are current now. We don't expect to have large settlements as we move forward and it's a good base rate for our Company as you model them into the future.

And then the last item which is more mechanical in nature, we do have a headwind associated with higher interest and a little bit in other. The interest is associated primarily with increased debt related to Infastech that we will experience throughout the year, although we will bring that down as the year closes. But it will spike throughout the year which will drive some additional interest expense in 2013.

So the last thing to mention is free cash flow. We expect free cash flow to be approximately \$1 billion in 2013, which is slightly down from the number I just reviewed for 2012, but let me walk you through that math.

In 2012 our free cash flow was \$1.060 billion, within that approximately was \$150 million of HHI free cash flow. So we backed that out as that won't exist, but then we have free cash flow coming in from Infastech which will be approximately \$90 million. That gets you right on that \$1 billion number for 2013 and there is a modest working capital turn improvement in it as well.

So let's move to the next page on little more clarity on some of the seasonality and geographical aspects of our guidance. First of all, seasonality. As all of you know, our first quarter tends to be one of our lower performance quarters from a volume perspective and it is slightly higher from a tax rate perspective.

We expect the first quarter will represent about 17.5% of our full year EPS, which is a slightly below our historical number of 18% to 19%, which goes back looking at the combined Company for the last six years. And it really is driven, as I mentioned, primarily by volume. We tend to see anywhere from \$150 million to \$250 million less revenue in Q1 versus the average revenue we experience through Q2, Q3 and Q4.

The other factor is that we are making the investments in these corporate growth initiatives that are very important to achieving our 4% to 6% long-term growth objective. They are front-end loaded, and so we will experience a little bit of a dilutive impact in Q1 and Q2 in particular that will cause a little more pressure to this historical percentage that I just provided. And as a result we think the 17.5% is a reasonable estimate.

Shifting over to a geographic view -- North America we expect to continue to see low-single-digit organic growth. We do think that we will continue to see the benefit of early stage of recovery in the US residential construction market. We saw a little bit of that in our CDIY business in 2012 with a 5% organic growth in North America and we would expect those types of trends to continue as we go into the 2013.

They will be slightly muted by a slower recovery in our Security and Industrial markets; however, overall we do expect low-single-digit growth in North America.

Europe, slightly better performance than we experienced in 2012, but not dramatically. Still I think we'll see low-single-digit organic revenue declines primarily in our Industrial and Security businesses while our CDIY or Construction markets will remain relatively flat.

And in emerging markets, low teens organic revenue growth, so somewhat consistent with what we experienced in 2012, but we will actually start to see that improve more as the year goes on as those organic growth initiatives that Jim reviewed really start to impact the top-line.

And then the last thing on the page is just reinforcing what we mentioned related to the organic growth initiative impact. As you know, there was a negative impact in 2012 of \$15 million as we started the investment process. It's \$65 million in 2013 with a negative drag of about \$30 million in 2013 or that \$0.15 EPS I mentioned.



The end result three years from now is we still expect \$850 million of revenue associated with this program incremental with \$200 million of incremental OM, which is approximately a 25% OM rate, significantly above our line average. Jim touched on the associated operating expenses and CapEx investments that we'll make over that time frame as well.

So on page 16 a little more clarity around the segments. First of all, CDIY, we do believe we will see mid-single-digit organic revenue growth, so somewhat consistent with what we experienced in 2012 and new products that we continue to introduce really allow us to increase the momentum in North America and grow in emerging markets and outpace any sluggishness that we really experience in Europe, which we expect to be a relatively flat performance in Europe.

The OM rate will increase slightly year over year due to cost synergies, but there will be a bit of a drag on the OM rate temporarily due to some of these investments in growth initiatives that we have touched on.

In Security we do expect a shift from a declining situation to a flat to low-single-digit growth in the Security segment in 2013 as modest growth continues to improve in North America. And we will be able to offset the continued low-digit growth that we would expect to see in Europe in a difficult market over there.

The operating margin rate will increase year over year due to cost synergies as well as carryover of some of the cost containment actions I touched on earlier.

And in Industrial, flat to low-single-digit organic revenue growth is expected. In our Industrial Automotive Repair tool business we would say relatively flat as we see growth in North America that is offsetting a continued weakness expected in Europe.

In Engineered Fastening we would expect low-single-digit growth as global light vehicle production continues to slow modestly and we would expect our business to be modestly impacted as well, but continuing to show growth.

And then operating margin rate will actually decrease slightly for industrial due to two things -- one, the addition of Infastech which is slightly below line average to start, but we would expect that it would get above line average as we get deeper into the integration process; and then some of the investments I mentioned on the growth initiatives as well. So growth in CDIY will likely outpace Security and Industrial and then we will see some nice operating rate expansion in both CDIY and Security.

So in summary, to summarize the presentation portion of the call this morning, we do think 2013 will be another solid step towards achieving our mid-decade vision with 2% to 3% organic growth, beginning to make investments associated with the growth initiatives and 16% to 20% EPS expansion associated with that.

Looking back at 2012, it was a transformational year for our Company. We divested a business, HHI, that was very successful, but we had concerns about the long-term strategic aspects of it.

We announced the acquisition of a wonderful company, Infastech, that we believe will be a great addition to our portfolio and ultimately drive a significant amount of organic growth and operating margin rate accretion over the long-term.

We increased our dividend 20% and we were able to repurchase \$200 million of stock over and above the HHI repurchases we commenced in late December of 2012.

The organic growth initiative programs have commenced in the fourth quarter of 2012. We do believe \$850 million of incremental revenue and to \$200 million of incremental OM will be achieved by 2015 and will allow us to reach that 4% to 6% long-term organic growth goal without relying on a macroeconomic environment that could be difficult over the next two to three years.



In addition, we have made a tactical pause and significant M&A in 2013 outside of some bolt-ons that we will do in emerging markets to help us accelerate our organic growth over the long-term. But the long-term capital allocation strategy remains the same -- still two-thirds of our free cash flow will be dedicated to acquisitions and one-third going back to the shareholders to dividends or opportunistic buybacks as appropriate.

It also allows us to enable a more laser focus on the organic growth and it facilitates our ability to continue to improve our CFROI and allow it to move into the middle of that target range we look for of 12% to 15% in 2013.

The Stanley fulfillment system really allows us to drive a lot of the things that we are doing. We saw benefits again in working capital in 2012. Jim touched on how we think it will begin to allow us to drive more organic growth in the Company. And we feel good that 2013 will be another solid step towards our mid-decade vision.

Kate Vanek - Stanley Black & Decker, Inc. - VP, IR & Government Relations

Lorraine, we are ready for the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Dan Oppenheim, Credit Suisse.

Dan Oppenheim - Credit Suisse - Analyst

Thanks very much. You talked a lot about the organic growth, but I was wondering about the CDIY. You talked about the operating margin to increase slightly with the cost synergies. You've done a great job in terms of looking at pricing centers there to help margins slightly. Is there further opportunity that you have there in '13 and beyond as you think about margins in that?

Don Allan - Stanley Black & Decker, Inc. - SVP & CFO

Yes, this is Don. I think 2013 for CDIY will continue to be a nice year of mid-single digit organic growth, has focused on more margin accretion related to the cost synergies. But it is also important to recognize that we do want to make sure that these growth investments are in place and begin to get an impact in the back half of 2013. So that will mute clearly the operating margin rate expansion to some extent.

But going forward, as far as looking at this business and operating margin rate, we do still see opportunity for further expansion and I think one of the bigger areas will be our ability to focus on these organic growth programs in emerging markets. If you look at the incremental operating margin rate, it is 25% associated with these growth initiatives; a large part of that is impacting CDIY. And so even if we do see price pressure in certain areas, overall, I do believe that we will be able to continue to expand operating margin rate.

Dan Oppenheim - Credit Suisse - Analyst

Great, thanks.

Operator

Stephen Kim, Barclays.



Stephen Kim - *Barclays Capital - Analyst*

Thanks a lot, guys. Yes, you spent a lot of time talking about the emerging markets opportunity and your approach to it. But I did have one additional question. You talked about opening up a few different plants. I gather these are probably going to be relatively small, mostly assembly-oriented, but I wanted to confirm that. And when you talk about opening up an Indian plant and expanding Brazil, maybe China and Turkey as well, I was wondering if you could be a little more specific about which countries you are thinking about prioritizing, particularly as it relates to opening up plants this year.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Sure, Steve. First of all, you are right about the plants being relatively small; there is no need to built monuments at this point in time. And the key for these plants is to keep the overhead down because the competitors don't have high overhead.

And some of our plants in the emerging markets that serve the Western markets have a lot more overhead than the local plants of competitors serving the local markets. So there is a very important element of that which is keeping the overhead down. It is really a different approach.

We have to have kind of the Western company mentality in terms of compliance with regulations and all those sorts of things and environmental and so on, but we cannot have the Western mentality as it relates to the overhead in the plants. So relatively small and a typical investment for something -- for a plant of this nature would be in the neighborhood of around \$10 million.

And then the other question in terms of prioritization -- interestingly when we look at the emerging markets, and 70% we think of the growth in the tool and hardware industry over the next 20 years is going to come from the emerging markets in our view.

And when look we look at where the growth is going to come from, we can start with the BRICs, that will be about a third; and then there is the next 11 headlined by Turkey and Indonesia, that will be another third, the next 11; and then all the other countries after that will be the last third.

So a strategy to go in and just serve the BRICs or China and India or even -- or something like that really won't get the kind of fast mover advantage that we think we can have here and it certainly won't capitalize on the opportunity. So unlike many initiatives where you say, okay, let's just focus on the 80% rule. Here you have to have a layered strategy. And we've got terrific infrastructure already in Latin America.

So when you look at the BRICs, for us it's really Russia, India and China -- in China clearly we will have a plant serving the local market plant or plants; we have one in India already, we may have another one at some point in time. And then Russia -- Russia you don't need a plant. Russia can basically import from China very cost effectively. There is no competitor that has a plant in Russia of any material size.

So that kind of covers the BRICs, then you start getting into Indonesia and Turkey. Presumably at some point we will have a plant in Turkey; it's not a top priority but it is something that we are obviously looking at and working on, and maybe in Indonesia. The rest of the next 11 can be served from the plant infrastructure that I just talked about.

And certainly the last third -- the strategy to go into those countries will be quite different than it will be for the BRICs and the next 11; it will be a far less intensive approach and more -- it will be much more of kind of an import model into those countries until they develop over time.

So, for instance, Africa is going to be incredibly important in the future, but it probably will be 10 years before we can justify a major thrust into Africa with plants and the whole nine yards of infrastructure.

Operator

Michael Rehaut, JPMorgan.



Michael Rehaut - *JPMorgan - Analyst*

I had a question about your outlook for Security in 2013, specifically in North America I believe you are looking for modest growth to be offset mostly completely by Europe. I was wondering if you could go into the growth drivers in North America for Security. And I think over time Security in general has been looked at as a higher growth opportunity as you have pieced it together over the last 10 years through different acquisitions.

Maybe first talk about 2013 drivers, what is working for you, what's maybe still an opportunity. And additionally, how the growth in Security in North America has played out over the last few years relative to your expectations.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Yes, I will take that, Mike. There is some level of granularity we are not going to provide on this call. But I think we have been fairly public. Remember you know well our Security business in general and North American business in particular is overwhelmingly commercial. About 20% to 25% of that business is driven by non-residential or commercial construction. That is the biggest driver, about another 15% is retail construction.

And as Jim pointed out, while commercial construction is improving from a very low base, we still don't anticipate for that to be a robust market. So what slowed down the growth of that business the last two or three years is quite frankly the complete lack of any commercial construction activity or certainly the reduction in commercial construction activity. And we do need new commercial construction to get the new accounts to prime the pump to generate the recurring revenue that is so important to that business.

The opportunities though are in areas such as where we are less developed such as healthcare, which as you know is an important small but emerging high-growth business for us that we report within our Security business. And with the acquisition of Niscayah, particularly in North America, the Niscayah team was very well positioned and has tremendous vertical market expertise in the financial and banking sectors.

That is two areas where up until now we had very, very little business and we think that we have the opportunity to grow in those areas irrespective of market conditions.

So you've got a commercial construction market that is anything but robust, but we think it will be a little better than -- it will be no worse than prior years. With the upside opportunity from healthcare, financial institutions, all other things very little change from prior years.

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

And I'll take a stab at kind of adding something to that which is we have done, as a Company, I think 70 acquisitions over a 10-year period and of those the vast majority have been in Security. And they have been all-consuming for the management team.

And we bought into what we thought was a high-growth market and normal -- under normal circumstances historically it has been both from a secular point of view given the importance of security growing and so forth and also just from the standpoint of being a technologically driven market that has a lot of innovation and value creating change going on within the industry.

So it is a high-growth market; it has been depressed by commercial construction over the years. But the key to growing and out-performing vis-a-vis the market, regardless of what size the market is at any point in time or growth rate it has, is to have differentiated value propositions.

And what I would say we did over the course of building the Security business was we assembled all the pieces that are required to provide differentiated value propositions to various industry verticals. So, for instance, healthcare, education, financial services, government, the global customer that wants to be served in a global fashion like an industrial or that type of organization.



So we have all of these pieces and one of the thoughts behind the hiatus that we went on in July was that we are not getting above market growth in Security and in order to do so we have to spend the time and focus the same people that have been focused on doing over approximately 50 acquisitions and focus them on organic growth and taking what we have and maximizing it.

And I just got back from a sales meeting from North America Security where they had every commercial person in the organization gathered in one location. And they have gotten to the point now where they have been able to take these value propositions that I have discussed here and now commercializing them -- in the process of commercializing them.

I've never seen in the security business a more charged up sales force than we have right now because they finally have what they need to grow and they are going to go out and do it.

So I would suggest that we are totally on the right track in terms of growth in the security business. We have -- if you look back you can certainly argue that it hasn't been what we had hoped for, but I'm very confident that it will be on a prospective basis.

Operator

Rich Kwas, Wells Fargo Securities.

Rich Kwas - Wells Fargo Securities - Analyst

I had a question on the Security longer-term on the margin. So you are around 15% to 16% right now. What is the progression to get to that -- back to that high teens rate? I think, John, you referenced you are going to need some macro strength in the commercial construction market, retail construction market. But other than that, is there anything that would prevent you from getting there over a two- to three-year period?

John Lundgren - Stanley Black & Decker, Inc. - President & CEO

Yes, the answer -- Don is going to give you a little more granularity, Rich. But remember Niscayah is a big piece of that now and it's way below line average margin. That being said, we have increased the Niscayah operating margin between 500 and 800 basis points. So part of it is simply math as Niscayah represents almost 40% of our Security segment now and the margins continue to increase. But I will ask Don to give you just a little more granularity than that.

Don Allan - Stanley Black & Decker, Inc. - SVP & CFO

Yes, Rich. If you look at -- obviously Jim reviewed the Q4 performance where he looked at the segment, it was 15.5%, but without Niscayah it was closer to 17.3%. So clearly the underlying business is still kind of in that 17% to 19% range that we are striving for in this business. And in the third quarter it was closer to the 19% number when you excluded Niscayah.

So it really comes down to our continued execution on the cost synergies of Niscayah and a combination of making sure that some of these growth initiatives, although Jim didn't go through as much detail on the ones in Security, but there are certainly some significant growth initiatives in the world of Security as well in that \$850 million.

That will allow us to stimulate more volume growth which ultimately will help us leverage the cost base and ultimately drive those percentages in that range of 17% to 19% with an average of probably about 18%. I really believe that this business base and its current makeup is in that category and it's more of a timing issue over the next few years.



John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Rich, I will remind you of one more thing. I know you are aware of this, but remind you and I think it's important for everyone else on the call. This business overall, more on the Mechanical than the Convergent side, does have a little bit of seasonality.

And historically if you go back in time you're looking at a couple hundred basis points lower margins in the first and fourth calendar quarters, a lot of reasons, we have discussed them, and more -- better margins in the second and third quarter. It is purely due to seasonality -- and so, as you are looking at long-term margins take a 12-month look and project forward.

And be careful projecting off a quarter, because I would argue that second and third quarter flatters our margins a little bit and first and fourth quarter depresses them somewhat artificially due to seasonality.

Operator

Sam Darkatsh, Raymond James.

Unidentified Participant

Thanks for taking my questions. This is Josh filling in for Sam. A quick clarification before my main question -- you said Niscayah was 40% of security segment sales in 2012?

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Well, take out HHI and add Niscayah, it's almost 50% of what is now remaining.

Unidentified Participant

50% of the remain, thank you. And then shifting gears to the Infastech acquisition, could you give us some color, if possible, on what is going on to delay the timing or why there might be risk to the close before February?

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Simply said, it's factors really beyond our control. China has a very methodical antitrust, believe it or not, approval process. We've done everything we can do, we are in the queue and simply said any acquisition is very, very thoroughly reviewed. And we see little or no risk.

As I'm sure you are aware, Chinese New Year, which starts in mid February, things do slow down a lot. So I believe there is an incentive on the authority's side to get that behind them prior to Chinese New Year and obviously there is an incentive for us to get it done.

But what our advisors tell us is we have done everything we can do, it is in good hands, it is going through a very normal and expected, albeit slow, approval process. But we don't see any -- there are no numerical activities or issues, it is just a question of time.

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Exactly. There is no reason (multiple speakers).



John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

100 -- 99.9% probability of closing. The question is purely on timing, if that helps.

Unidentified Participant

Thank you for the color.

Operator

Dennis McGill, Zelman & Associates.

Dennis McGill - *Zelman & Associates - Analyst*

Two questions kind of related to the longer-term targets that are intertwined. The first is on the ROCE target of 15%, can you just tell us what that is today or what that was in 2012 and how you guys calculate that? And then relative to the 4% to 6% organic growth target for the whole Company, how would North America look within that target range?

Don Allan - *Stanley Black & Decker, Inc. - SVP & CFO*

Yes, the ROCE at the end of 2012 was about 10.5%. And Kate can send you the details of the calculation because it is not exactly clear cut. But it is relatively consistent with what you would expect with an ROI calculation with some adjustments for after-tax interest and amortization in some cases.

So when we look at that and we say how are we going to get that to 15%, we clearly think that we will get a significant improvement in 2013 just from the fact that we won't be doing any significant acquisitions. And we will continue to show significant earnings improvement with almost 20% EPS growth in that time frame. And so, we would expect probably almost a 2 point improvement in 2013 from that level.

The associated CFROI, or cash flow return on investment, at the end of 2012 was about 12%. And so, there is about a 2 point or 1.5 to 2 point gap between ROCE and CFROI and that is primarily due to the intangible amortization that we experience through a lot of these non-cash expenses through the acquisitions that we've done over the last eight years. And we would expect a similar result in there. That would improve probably 1.5 points to 2 points as well in 2013.

And so, we feel like we are on track to really move that forward and both those ratios, getting them in that 12% to 15% band, even ROCE probably in 2013. In North America it is likely going to be a little bit higher than the line average for the whole Company. But we don't exactly do a precise calculation.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

North America [we do on] revenue, we do it on organic growth not on ROCE -- of the 4% to 6% organic growth.

Don Allan - *Stanley Black & Decker, Inc. - SVP & CFO*

Yes, I mean the 4% to 6% organic growth in North America, I would say that that is probably -- when you look at that over the long-term, I would say that you are probably still looking at a couple points of growth frankly in North America. And so, the bulk of the growth is going to come, I would imagine, in emerging markets over the long-term.



Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Yes, if we can get the core growth rate in North America to 2% to 3% the 4% to 6% is very achievable.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Because it is 50% of our volume.

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Yes. And just one other thought on the ROCE and the cash flow return on investment -- the ROCE for us over the years has become disconnected from the cash flow return on investment because of our acquisitive activity and the amortization that is associated with it. It's really -- I mean for those that are familiar and have studied it, it's really more of a book income concept than it is a cash income concept.

And we are evaluating -- as a management team right now we are evaluating moving to more of a cash flow return on investment view, because it actually is more relevant to our business today because our cash earnings are substantially higher than our book earnings. And we are going to discuss that at our next Analyst Meeting, which will occur sometime in the middle of the year, date to be announced.

So we will have more on that. But I think cash flow return on investment is increasingly more relevant to measuring the return on investment of this Company.

Operator

Ken Zener, KeyBanc Capital.

Ken Zener - *KeyBanc Capital - Analyst*

A quick question, the 17% -- or just if you could address this -- the 17% EPS in 1Q compares to 22% EBIT mix last year. So if there is any outlying driver, if you could address that briefly.

But with Niscayah, because it is such a large piece of the business could you update us where we are in the transition? If I think about HSM, the reverse integration that you did, you are sloughing off low margin install business as you transitioned to a more recurring revenue mix. Can you highlight the challenges and successes you've faced in that relative to the economic stress that we have had? Thank you.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Yes, I will address the Niscayah while Don racks his brain and tries to figure out the answer to your other question.

Ken Zener - *KeyBanc Capital - Analyst*

It seems -- the EBIT mix is lower.



Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

You know, we have owned Niscayah something like 16 months now and when we bought it, it was one of those -- it was a contested situation. So we didn't have the normal opportunity to go in and vet the management team thoroughly like we would with an uncontested transaction.

And so, the hope was that we were going to get some good people at the headquarters and that we were going to be able to take our basic prop business processes that we have in North America and implement them in Europe in fairly short order. And what we found was that we had strong country managers for the most part in Niscayah, which was good. But we also found that the centralized management team was quite weak.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

In Europe. (Multiple speakers) country managers in the US as well.

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Yes, yes. So in any event -- yes, well, everything I've said thus far relates to Europe and we will talk about North America separately. So, we put a Stanley leader in charge of the business, he replaced the entire management team within about four months after ownership. And they have gotten great traction and they have out-performed their cost synergies and now they are really focused on growing the business in a tough environment.

One of the challenges with Niscayah was -- from a growth perspective in addition to the environment, was the fact that a fairly significant percentage of their revenue came from referrals from Securitas. Because they were -- at one time Securitas and Niscayah were part of the same company and then they were spun -- Niscayah was spun from the parent.

And they still had a symbiotic relationship because Niscayah was the electronic business and Securitas was the guarding business. And so when a customer needed electronics they were referred over to Niscayah. So we had to kind of fill the gap there in the revenue that no longer comes from Securitas because they were the ones that we contested the acquisition with, so they are not our friendliest allies out there in the marketplace.

So I think the management team has done a fabulous job when you think about the revenue being down about 5% on the average this last year organically, filling the gap for the lost business from Securitas as well as dealing with a difficult market in Europe. And it's very stable, they are going to perform at or above the cost synergy targets and the acquisition is going to drive every bit of return that we thought it would.

And in addition to that it has really enabled us to be a global Security franchise. We are really the only commercial Security company in the world that can coordinate globally now, which is a big advantage.

So all of that is a good story, it's a tough environment, we bought it right before the European market issues were manifested. However, we expected that, we anticipated that. And so, I think in the end this is going to be a terrific acquisition. The operating margins are about double what they were when we bought it now and they are moving on up again and this year as well. So it is all in a pretty good place.

The North American piece I think was for the most part a pleasant surprise in the sense that -- I talked earlier about these value propositions and the verticals and so forth. They brought in North America great strength in these verticals.

So they had a vertical market approach in North America, they were relatively subscale, but they managed to do quite well with their business despite that because they have such strong vertical value propositions. We have taken those and we have now integrated them with the commercial force in North America, which has given us an advantage we think in the marketplace, especially as we pursue these organic growth initiatives.

So I think on balance we are very happy with Niscayah. It would have been better if the public relations aspect of this buying a European company hadn't occurred two months before Europe went into a deep-freeze. But nonetheless we anticipated that, we have it all built into our pro formas and it's going to be a great acquisition, it already is.



John Lundgren - Stanley Black & Decker, Inc. - President & CEO

Just one final point, Ken, on Niscayah and Jim touched on it. Two points I think just to close the loop because the last thing we would want to leave is any impression that the integration thus far has been anything but a terrific success. We are completely satisfied, more than satisfied with the acquisition and what it does for us.

But the first point Jim made, an important one, we normally hit the ground with our feet running 90 days before closing. And simply said, the integration process started on closing because it was a contested public acquisition of a public company.

We are on schedule, we just started three to six months later than we normally are allowed to start. Second, Jim referenced North America and subscale (multiple speakers) great franchises. Only 15% of the business is in North America, but upwards of 30% of the synergies came from North America because we were able to consolidate, as Jim suggested, and address that subscale issue. Don, you've got a view on the calendarization of EBIT?

Don Allan - Stanley Black & Decker, Inc. - SVP & CFO

I sure do. So the answer to the question, Ken, is, as I mentioned, 17.5% of our total EPS will happen in Q1, which is slightly below when you look at the historical trends. It's a couple factors -- when you look at Q1 last year our operating margin for Q1 represented about 22% of the total year operating margin, which is close to the EBIT number or EBITDA number you were mentioning. And this year we would expect that operating margin number to actually be closer to 20% of the total for the year in Q1.

Why is there a difference? Well, the main difference, frankly, is these investments we're making in growth. As I touched on, we do have a dilutive impact for the year, the bigger part of that dilutive impact happens in Q1. And it begins to moderate as we get into Q2 and starting to flatten out in Q3. So that is a driver associated with that.

And then the other area would be in the area of interest and tax. So we will -- our interest will spike, as I mentioned, due to the Infastech transaction temporarily throughout the year. We will see that happen initially in Q1 and then begin to work its way down as the year goes on. And then in addition to that the tax rate -- we did have a modest tax benefit in Q1 of last year that's also affecting that that we don't expect to repeat.

Operator

Mike Wood, Macquarie.

Mike Wood - Macquarie - Analyst

Could you elaborate on the road map or experience you've had in the past with the mid-price point product that gives you the visibility that you can gain share and achieve a 35% gross profit margin without bringing in more price competition from the people that you are taking the share from?

John Lundgren - Stanley Black & Decker, Inc. - President & CEO

Yes, I think it's as simple as -- and I think Jim described it pretty well. We are familiar enough with the end markets that we understand the features that people will pay for and they won't. And our history with a product that was successful at lower margins was quite frankly we were -- I will use the not so elegant term of the dumbing down products produced for the West by taking cost out to get to a price point where it would sell.

The new approach, and it is a pervasive effort across our Company of designing to value what product tear down, what will an end-user pay for, what does he value and what does he not value. So simply it is re-engineering these products from a clean sheet of paper as opposed to trying to just take cost out of a higher cost product produced with more features and benefits for a market that it wasn't designed for.

And as Jim said, to do that we need basically a zero base or clean sheet engineering approach, which we have invested in and it's part of the investment that Jim alluded to.

And secondly, we need to produce it locally in plants. They're going to be -- they're certainly going to be capable -- not capable, they will adhere to Western EH&S standards, some of them are already our plants. But with a lot less overhead, a lot less infrastructure than some of the plants designed to produce premium price products in low cost countries but to export to Western markets.

So the combination of design for local market needs and produced in local markets will give us a tremendous edge and this is something we have got a lot of experience with. We know what the price points are in the market, so we are beyond cautiously optimistic, we are confident that this approach is going to yield the kind of results we are looking for.

Jim Loree - Stanley Black & Decker, Inc. - EVP & COO

And in addition to all that, we have looked at a number of companies that do this and in terms of business development activity. And I can tell you that their income statements and their cash flow statements and so forth when you consider the things that we know in the synergies that we can bring to that sort of business model.

We -- there is an existence theorem, and I think it's really important because what John described was 80% to 90% the theory of the case. But we have examples in the emerging markets of business development targets that we have looked at that can get there, and so we know it can be done.

Operator

Jason Feldman, UBS.

Jason Feldman - UBS - Analyst

Thank you for all the detail on the strategic growth initiatives, it was very helpful. But when we think about those organic growth initiatives as you kind of stretch to get to the 4% to 6% long-term organic growth range, do we need to start thinking about incremental margins differently kind of an ongoing structural basis? Or do you view these kind of up-front initial investments as more kind of one time in nature and then ultimately we'll kind of get back to the incremental margins that you have targeted historically?

Jim Loree - Stanley Black & Decker, Inc. - EVP & COO

Yes, the organic growth has the ability to drive operating leverage in the Company. So while there will be some investments, the investments for the most part are simply the operating expense that kind of goes with the gross margin in order to get a certain contribution margin.

In some cases if we are building a plant and so forth there will be some additional fixed costs. But I would say that we fully expect the emerging market element of this to be overall rate accretive to the Company even with all those investments very quickly. So it will be a net positive for operating margins over the long-term for the Company from the emerging markets.

And then most of the other things that we are doing are very much relying on existing plant, existing facilities, we are adding salespeople for the most part, commercialization people, that is going to be more incremental at the contribution margin line based on what we do today.



And in most of these initiatives we're -- as you walk through them, in many cases you will see that every one of them has a specific value proposition associated with it. And we are big believers in that the stronger the value proposition the more you can get paid for something. And we are very much interested in value pricing these as we go forward.

Jason Feldman - *UBS - Analyst*

Thank you.

Operator

Eric Bosshard, Cleveland Research.

Eric Bosshard - *Cleveland Research Company - Analyst*

The -- I think hand tools you kind of were flat in the quarter which related to you walking away from some lower margin business. I'm curious as you look at 2012 and 2013 how you look at the marketshare performance of hand tools and what you see going on inside of that business?

Don Allan - *Stanley Black & Decker, Inc. - SVP & CFO*

Yes, I would say that John articulated us walking away from business which was a very intelligent decision by our CDIY team. As you know, we look at different pieces of our business and make sure that we are achieving certain levels of profitability and pricing associated with that.

But ultimately we also are very aggressive around new product innovation and technologies that help us drive growth as much as possible. And when I look at the hand tools business, it will be a business that will continue to grow. And when I think about CDIY in 2013 growing mid-single-digits I don't see why hand tools wouldn't be very close to that type of growth in 2013.

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Which would imply a modest share gain.

Don Allan - *Stanley Black & Decker, Inc. - SVP & CFO*

Which would imply a modest share gain. And it also would imply that we continue to drive activities in emerging markets that will help that global growth number as well.

Eric Bosshard - *Cleveland Research Company - Analyst*

Thank you.

Operator

Peter Lisnic, Robert Baird.



Peter Lisnic - *Robert W. Baird - Analyst*

Can you give us a little feel for the implications for the change away from the direct model and US Mechanical access? Just kind of discuss the strategic implications there and what that might mean for what I thought used to be at least, or might still be, one of the highest return profiles business wise in your portfolio.

John Lundgren - *Stanley Black & Decker, Inc. - President & CEO*

Sure, Pete, it's a great question and I think Jim gave a great start to answering it in his prepared remarks, so I am going to kick it to him. But importantly, it is a conversation that we spend a lot of time internally having as a corporate management team and with Brett's team. But Jim, why don't you just elaborate a little bit?

Jim Loree - *Stanley Black & Decker, Inc. - EVP & COO*

Yes, I think now is a great time to do it, number one. It historically has served Best quite well because if you go back to the -- I think it was the 1930s when Best kind of came into existence. They had a patented product that was the interchangeable [core] that played extremely well in certain segments of the market like healthcare, education, government and so on.

And as the market evolved over the years they had the direct model and the two -- our largest competitors had a distribution oriented model. And as the economy slowed down and construction slowed down over the last five years or so the distributors, with their profit margins under pressure, began to look more and more at other ways to grow their business and to grow their profits. And they started becoming more aggressive in some of the markets that were traditional home territory of Best.

And today we are not dealing with a proprietary interchangeable core anymore, the patents have all expired and so forth. So, our sales force was largely accustomed to being sort of -- had a farming mentality, if you will, in serving these customers and did a lot of transactional support for the customers and so forth, things that distributors do very well. But they weren't out there with the size and scope of go-to-market resources that the distributors were.

And we did have the advantage that we could cover multi-geographic locations more effectively with a direct model, but it also was more expensive.

And so, when we looked at this change we think this is a moment in time when we have enough value to add to the distributors in the sense that we have an installed base, very valuable. And we have extremely robust new product development for the first time during our ownership of Best access, especially in the mid-price point product which has become extremely important in the -- with the economic issues that are going on today.

So for us to get to the construction market we felt we needed to make this change and we felt that it is always somewhat risky in an entrenched distribution model. But we believe this is a moment in time when we have enough value to add to these distributors that we can partner up with them and put away the competitive aspect that we have had that has always made it difficult to work -- to coexist with the distributors with kind of a hybrid model that we had.

And we have taken a lot of cost out of the field in order to account for the somewhat lower gross margins that will be associated with this. And so we think it's income neutral from the standpoint of making the change because of the cost take-outs and we think that this will enable us to really charge up the organic growth in the MAS model. So we still believe that it will be a great return business on a go-forward basis, but we think it will be a higher growth business.

Operator

Thank you. (Technical difficulty), Janney Capital Markets.



Unidentified Participant

You have had a great deal of success on the working capital management side, it has been a focus and obviously the cash flow is reflected in that. With a lot of effort in the growth of emerging markets how does that affect your working capital management forecast?

Don Allan - *Stanley Black & Decker, Inc. - SVP & CFO*

Yes, I would say that -- I wouldn't see it having a significant impact on working capital. We still feel very passionate that achieving 10 working capital turns by the middle of this decade is achievable. And all the initiatives that we are looking at in emerging markets we don't expect to impact that objective.

Now that being said, we probably will end up carrying a little more inventory in that part of the world to make sure that we meet the needs of customers. But when you set the impact as a percentage of the whole Company, it's not going to be more than a 10th or two of an impact across the whole Company. And it doesn't really impact our objective of getting to 10 working capital turns.

Unidentified Participant

Great, thank you.

Operator

Thank you. Do you have any final remarks at this time?

Kate Vanek - *Stanley Black & Decker, Inc. - VP, IR & Government Relations*

No, I just want to thank everybody for logging in today and participating. Please let me know if you need anything in the way of follow-up.

Operator

Thank you. And thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating; you may now disconnect.

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