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SWK - Q1 2013 Stanley Black & Decker, Inc. Earnings Conference Call

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OVERVIEW:

Co. announced 1Q13 diluted EPS excluding charges of $1.03, and GAAP diluted EPS of $0.52. Guidance was given for 2013 EPS of $5.40-5.65.

CORPORATE PARTICIPANTS

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

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

Jeff Ansell *Stanley Black & Decker, Inc. - SVP and Group Executive, CDIY*

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

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

CONFERENCE CALL PARTICIPANTS

David MacGregor *Longbow Research - Analyst*

Dennis McGill *Zelman & Associates - Analyst*

Mike Wood *Macquarie Research Equities - Analyst*

Eric Bosshard *Cleveland Research Company - Analyst*

Jeremy Kaprin *CLSA - Analyst*

Liam Burke *Janney Capital Markets - Analyst*

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

Jeffrey Kessler *Imperial Capital - Analyst*

PRESENTATION

Operator

Welcome to the first quarter 2013 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 a 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 the Vice President of Investor and Government Relations, Kate Vanek. Ms. Vanek, you may begin.

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

Thanks so much, Lorraine. Good morning, everybody. Thank you all for joining us this morning for Stanley Black & Decker's first quarter 2013 conference call. On the call in addition to myself is John Lundgren, Chairman and CEO, Jim Loree, President and COO, Don Allan, Senior Vice President and CFO, and Jeff Ansel, Senior Vice President and Group Executive, CDIY. 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.

The replay of the call will begin today at 2.00 p.m. Replay number and access code are in our press release. This morning, John, Jim, Don, and Jeff, will review Stanley's first quarter 2013 results and various other matters, followed by a Q&A session. Because of the size of the queue, we are going to be sticking with just one question per caller. As always, please feel free to contact me with any sort of follow-up questions that don't get covered during the Q&A portion.

As I normally have to do, we are going to be making some forward-looking statements during this the 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 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 Chairman and CEO, John Lundgren.

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

Thanks, Kate. Good morning, everybody. And thanks for joining us this morning for our first quarter earnings call. Just as a top line summary, despite a slow start to the year from a volume perspective, we exited the first quarter '13 with a lot of momentum that you will hear from Don later gave us confidence that we will achieve our fiscal year previous guidance and targets from an income perspective. Revenues increased 3% and that was largely due to the inclusion of Infastech which closed in February. That acquisition actually took several months longer to close than normal as we waited for various Asian government approvals. So we didn't get as much benefit in the first quarter as we expected. But the extra time really allowed us to hit the ground running. And that integration is progressing very smoothly and on or ahead of schedule now that we've started.

The organic growth initiatives that we have talked about in past quarters, they gained traction at an encouraging rate but our core business, organic growth did decline. Volume was down 1%. It was due primarily to a slow start to the North American outdoor product season combined with temporarily soft markets in Latin America, and modest continued contractions in Europe. A bright spot with CDIY operating margin expanded 160 basis points despite flat organic growth and we do remain on track for mid single digit organic growth for the fiscal year, and as Kate said, we have Jeff Ansel, our Senior Vice President, Group Executive responsible for that business to give you a little more insight on that a little later on in the call.

Organic growth in Mechanical Security did -- was offset by some declines in convergent Security in Europe. And as a consequence, our Security segment profitability was temporarily pressured by installation mix and volume declines primarily focused in the Nordic region, historically a very strong region for the legacy Niscayah business. And moving on to the Niscayah, the 2013 synergy estimate has been increased by $15 million. The total program estimate we're now taking a second look at it to think that we may even be able to get more, not this year but next year in 2014, as we combine that business with the former Stanley Black & Decker convergent Security business in Europe. 1Q diluted earnings per share of $1.03 was up 5% versus prior year. On a GAAP basis, EPS was $0.52. And as I suggested, and Don will give you more insight, we are reiterating fiscal year organic growth EPS and free cash flow guidance.

Let's take a quick look at our organic growth initiatives which as suggested they're on track to contribute about a point, 100 basis points of organic growth for this year. During the first quarter, we invested an incremental $16 million in spending. And a lot of that was in feet on the street, 370 new associates hired with about two-thirds of them, 225, in the emerging markets where we believe our greatest opportunity for growth is. Growth and volume leverage rests. All of the initiatives are tracking to their three-year goals, and as previously stated that is $850 million in incremental revenue and $200 million in incremental profit.

Well, let's take a look at some of the markets drilling down into some of the geographies. We are going to spend less time on geographies in general than we do historically. That is in your appendix, or will be in the appendix. But if you see all of the emerging markets, with the exception of one, a large one, showed very, very strong increases. Russia plus 19%, China 13%, Northeast Asia 13%, Turkey 12%, Southeast Asia, 7%.

Latin America experienced I will say what we believe is a confluence of temporary issues and they're different in each country, Brazil, Argentina, Venezuela, and Columbia. But as a consequence, our largest emerging market group, Latin America, where we have very strong market positions is actually down 2%, which we think is temporary. So that gave us a combined total of plus 2% in our total emerging market group, which is below where it has been historically and below where we believe it will be as the year progresses, and certainly an ongoing basis. Let me turn it over to Jeff Ansel, who as I said is the man in charge of our CDIY business and he's got some fairly exciting opportunities in his business that he is going to give you some more detail on.

Jeff Ansell - *Stanley Black & Decker, Inc. - SVP and Group Executive, CDIY*

Thank you, John. Looking at the CDIY results for 1Q, total revenues plus 2% driven predominantly by the Powers acquisition, organic revenues flat. As you can see in the upper left, our PPT or our DeWalt business, positive. It was however pressured in the quarter due to intentional promotional timing change, moving promotions that occurred in Q1 2012 to Q2 and Q3, 2013 to match the building seasons in North America and Europe, intentionally done as well. Cordless products performed very well in the quarter, pervasively. From a CPG or a Black & Decker perspective, positive from a power tool perspective. The outdoor season began late and thus pressured the results but overall positive results in the Black & Decker business. With growth primarily attributed to new products including Matrix, GYRO, et cetera.

In our HT&S business or our Hand Tool business, exceptional growth in our DeWalt hand tool range was really offset by weakness in Europe, Brazil, and Columbia during the quarter. If you look at the center of the page, you can see the track record over the previous four quarters of on average mid single digit growth, with this quarter being flat. The two reasons are outlined in this portion of the chart. Outdoor, given a four-week late start, due entirely to weather, put two points of pressure into the quarter.

The Latin American business, as John referenced earlier, added 1 point of pressure, so sans those two things we would have had consistent growth with previous quarters. We do feel good about the correction in the outdoor season which I will come on to in a few minutes. And the Latin American business was trending quite positive during the course of the quarter. It essentially just took a little longer to sell through inventories from 2012 than expected, about six weeks longer. So you can see the depiction for January was down 15%, February, down 6%. March rebounded very nicely to plus 15%. So really the first half of the quarter was pressured, the second half of the quarter was much more consistent with our previous results in Latin America. And finally, in the upper right portion of the chart, you can see the profit rates expanded by 160 basis points driven by mix, cost synergies and promotional timing to a record 14.5% for the first quarter.

Turning to the following page, I want to reiterate as strongly as I can our commitment and confidence to mid single digit growth for the year, even with the flat first quarter. Why do we have such confidence? Well they're depicted here. Five reasons primarily, first is around emerging markets, we believe we will have continued strength in Asia and other emerging markets which were up mid double digits in the quarter. Along with the Latin American recovery that I just outlined that has already begun. Additionally we added 185 sales and product head counts during the quarter. That investment combined with investment in programming from emerging markets will certainly improve our business sequentially as these resources and programs gain traction over the course of the remainder of the year.

Number two, reason for confidence is new product development. We have very robust power tool, hand tool, and home product, new product plans. The launch cycle for new products really begins in March, through October. So very little impact in the first quarter, but much greater impact over the coming portions of the year. A couple of examples to highlight. In March, we launched the world's first cordless, brushless framing nailer. That product competes extraordinarily favorably with anything that exists in the marketplace. It is the first framer to use cordless battery technology. It does not require disposable fuel cells which is a negative to the user and it works in any climate, any temperature which is also unique.

Based on the initial response to that product, we have doubled and are working to triple our capacity for that product for the remainder of this year. Additionally, we have really strong momentum in our DeWalt hand tool range. Up about 30%, as the trend line goes. And then our new steam products, which have led us to the number one position in Europe, continue to drive growth. So things like that really give us great confidence, and in general, our cordless business outperforming the market, while being number one, is another reason for confidence in the terms of new product development.

The third area of the outline is promotional planning. Programming for 2013 essentially starts in Q2 and Q3, versus Q1 of last year. We intentionally moved the timing of these promotions to coincide with the building season in Western Europe and North America, because those investments in Q2 and Q3 versus Q1 will provide greater ROI for our customers and for ourselves. So we feel very good about that and that led volume strength for the coming quarters.

Fourth, the outdoor season. The analytics have told us recently that April would be the kickoff to this season. We have seen that to be true. Last year, the outdoor season began in week 10. This year, the outdoor season began in week 14. So essentially we lost a month in the outdoor business, which occurred in Q1. The point would be though that the duration of the outdoor season is the same length regardless of when it starts. It will run five months. The starting point varies, so we will now run from April to August, versus last year, March to July. It is very consistent year-over-year. We have very strong cordless and corded listings across our enterprise so we feel very good about the uptick once the season does begin. And on average, temperatures globally were minus 11 degrees from where they were this time last year. A lot of reasons why this season is starting late.

And then fifth and final, but not least, is we had really strong revenue synergy plans continuing through the year. We will unveil for you one of these major or mega programs at our meeting in June. Subsequently, we have another mega launch in the third quarter. Both have confirmation with customers and channels in the market already. We just don't talk about those things until they're in the market and we will show you again two major programs and one in Q2, one in Q3, with a lot of activity there with really good traction.

So in closing, strong profit, improvement in the quarter, plus 2% total growth, flat organic sales, but with a track record of organic growth in the mid single digits, as depicted on Q1, we believe we have a really strong prospect in front of us. Organic growth head winds in the quarter were clearly timing and clearly temporary. We remain committed to the growth elements in emerging markets with lag already recovering, with new product development really starting in March running through October. Promotional activity as a tailwind in Q2 and Q3 versus a headwind in Q1. The outdoor season starting as we speak, albeit later than last year and really compelling revenue synergy plans that are built and ready to execute. So, we reiterate our confidence in mid single digit growth through the remainder of 2013. Thank you.

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

Okay, thank you Jeff. Exciting story there and all the more exciting because we really didn't even talk about a recovering US housing market, which as we speak is indisputably taking place. So, no reliance on that, but certainly that's going on as well.

Let's turn over to Security now. Overall revenues were $599 million, versus $592 million a year ago. Organic growth was minus 1%. And despite an OM rate of 10.3%, even lower than normal for first quarter, there were some very positive developments in Security during the quarter.

Let's start with organic growth which was very solid in several US-centric businesses, including Electronic Security, which was up 3%, Mechanical, which was up 5%, and Access Doors, which was up 4% organically. Europe, while not surprisingly under some volume pressure will outperform it's 2013 synergy commitment by $15 million, as John mentioned. Thus protecting full-year operating margin and ensuring the Niscayah acquisition produces a solid return on investment. Now, some of the CSS or Electronic Security volume growth has come at the expense of OM rate in the first quarter. And I believe we are at an inflection point where the exciting new vertical solutions in K through 12 education, health care, financial services, and retail, are ready to be deployed, and with a differentiated value to be sold, we are training and reinforcing a value-pricing mind set with the field which we will address this issue in addition to some other margin improvement actions that the team is taking. So we expect to see flat to positive organic growth for the year, with overall operating margins slightly positive year-over-year. And growing growth momentum heading into the second half in 2014.

Moving to Industrial, Industrial is also pressured by Europe. Especially in Industrial and Automotive Repair. Total revenues were $695 million, versus $662 million a year ago, organic growth was minus 1%. The profit rate was 14.1%, it was pressured by lower volume on the higher margin European business, cost absorption issues, and investment in the organic growth initiatives.

Now, as we take them business by business, Industrial and Automotive Repair, organic revenues were down 4%. The US was flat. Europe was down 9%. The good news here is the comps for both Europe and the total business ease as we get into second quarter and beyond, second half of the year as well. In the US, a strong MAC Tools performance was offset by weak government business and industrial MRO business for the Proto business.

I would like to highlight one of our organic growth initiatives, the smart tools and storage or otherwise known as Advanced Industrial Solutions, was up 5% organically. With CribMaster up double digits on vending success in MRO. In Engineered Fastening, they were flat organically. The Automotive business grew 6% outpacing a 4% decline in global light vehicle production. The North America Auto business was up 7%. Europe was up 2% as auto-related market share gains offset declines in Industrial, and a $5 million shipment timing issue which was customer-driven and pushed $5 million of revenue into the second quarter, at the expense of first quarter revenue.

Japan with its difficult situation in the auto industry was down 8%, on a 16% light vehicle production decline. And as John mentioned, the Infastech acquisition closed on February 27 and the integration is progressing well. This exciting new addition to the portfolio will add significant growth potential through emerging market and electronics content. And then infrastructure really was a bright light in the quarter as the offshore pipeline business drove 9% organic growth in CRC, a very positive sign, as the US onshore business is gaining cyclical traction. And the offshore business continues to grow. So stay tuned for a very strong 2013 for CRC Evans. Now I will turn it over to Don Allan who will take you through the financial aspects of the quarter.

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

Thank you, Jim. I would like to start on page 10 and talk about our free cash flow performance for the first quarter. There are really three things that I would like to point out. You can see that the performance was a negative cash flow of $132 million, slightly worse than our anticipated results, and let me walk you through some of the details associated with that. The first of which is working capital. As most of you know in the first quarter, we tend to see a sequential decline in our working capital turns, which we did see from the fourth quarter to the first quarter, from 7.5 turns in the fourth quarter, to 6 turns here in the first quarter. That was about a half turn lower than our expectation. And it is really being driven by a couple of things.

First of all, the lower overall volumes, in the first quarter, as well as the timing of the revenue within the quarter. As you have heard in various pieces of the call this morning, January and February were very slow in certain parts of the Company and then March began to accelerate and we saw improvement. That timing dynamic certainly caused pressure for the working capital number. The good news is that is a temporary phenomena, we don't see that as any major concern for the year and we still believe for the year we will have modest working capital turns improvement year-over-year.

The second item of note is other. Other is an area that always in the first quarter we see a large negative outflow. That's where annual rebates, bonuses, et cetera, get paid and that impact is reflected there. And then CapEx, slightly higher versus the prior year as we expected, due to certain growth initiative investments we're making as well as other key investments around our overall strategy. We still expect CapEx as a percentage of revenues to be about 2.5% to 3% of annualized revenue this year. So the first quarter performance, although a little bit worse than we anticipated, we are not concerned -- we believe that these are temporary issues that will subside and correct themselves in 2Q and we will still be able to achieve $1 billion of free cash flow for the full year.

So with that, I would like to move to page 11, and talk about our guidance reiteration for 2013. We believe that we will still be within the range of $5.40 and $5.65 EPS for the full year. That will be 16% to 21% EPS growth versus 2012. The factors on the left side of the slide indicate the items that we are reiterating associated with the certain assumptions within this range. The first is organic growth. We still believe we will grow 2% to 3% versus 2012. And the dynamics within that are consistent with what we said in January where the core business will grow 1 to 2%. And our organic growth initiatives will yield a point, but they will be dilutive by $0.15 to EPS.

The cost synergies associated with BDK of $0.23 and carry over cost reduction actions of $0.15 are consistent with January. And then Jim touched on as well as John the Infastech acquisition. We still believe the accretion will be $0.20 for the full year and even with a one month delay in the timing of the closing. Our share repurchase has gone successfully with $0.37 benefit. That will be completed in the coming weeks. And be behind us. And that's really associated with a large portion of the proceeds received from the HHI divestiture.

Moving over to the right side of the page, there is a few items that are changing but do have a neutral impact. The first of which we've mentioned a couple of times this morning that we believe the Niscayah cost synergies will be $15 million higher in 2013, now $50 million for the year. That is offsetting some of the volume and rate pressures that we're seeing in the CSS business. So a net neutral impact.

And then there's three additional items that are neutral as well. A small change in our other net assumption which is causing a positive of $0.05 versus our January guidance, tax rate is still within the range of 23% to 24%. But is trending towards the low end of the range. That will be a slight positive as well. And then we have a little bit of pressure in our shares outstanding. Our outstanding share number is expected to be slightly higher.

Moving to page 12, a few more assumptions associated with our guidance. On the segment side, you have heard from both Jeff and Jim some of the assumptions associated with the full year. For CDIY, we are very consistent with what we said in January. Still believe that our organic revenues will be mid single digits. We expect the OM rate to expand year-over-year as we see continued benefit of synergies, as well as incremental profit associated with volume. And a slight offset associated with some of the investments related to our growth initiative.

Security, similar story to January as well. Flat to below single digit organic growth. Although we have a mix in the geographies where we will see growth in North America, with offsetting pressure in the European markets. We do expect our OM rate to expand slightly year-over-year, as we will execute more cost synergies related to Niscayah as well as carry-over of some of the cost actions from last year.

And then in the Industrial side, flat to low single digit organic growth as well. Similar dynamic in the geographies where we see growth in North America. However, retracting environment in Europe that is partially offsetting that. And then the OM rate will slightly decrease year-over-year in this segment as we see a temporary impact from Infastech margins being below line average as well as the investments in growth initiatives.

The one last item I would like to mention associated with guidance is looking at the first half and the second half associated with EPS. Due to the growth investments that we have engaged and made, starting at the end of 2012, and the timing associated with the dilutive impact of that $0.15, the vast majority of that $0.15 dilutive EPS impact will happen in the first half 2013. And will have a neutral impact from the growth initiatives in the back half of the year as they begin to turn accretive and we expect them to be significantly accretive in 2014. That creates a dynamic when you look at the first half versus the second half where we expect the second half to represent 60% of the full-year EPS. I.e., the first half will be 40%. That's slightly off historical trends where if you look at the last three years of our Company, the second half has tended to be between 56% and 58%. The main difference between that and our expectation this year is these investments in the growth initiatives and the timing associated with that.

So overall, we believe that we will continue to see -- we will see solid growth in CDIY in mid single digits. That will outpace Security and Industrial. As we begin to see growth in the residential end markets, that is outpacing the commercial and industrial markets. With that, to summarize the call, I will pass it back to John Lundgren.

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

Thanks, Don. Just to wrap it up, hopefully it is clear that we remain focused on driving our organic growth initiatives and efficiencies across the Company. Maximizing the synergies across our lines of business, and certainly allocating capital in ways that provide excellent returns for our shareholders. We are reiterating full-year organic growth EPS and free cash flow guidance. The organic growth initiatives are gaining traction, and are on track to achieve our 3-year targets of approximately $850 million in organic revenue and $200 million in incremental operating profit.

CDIY, as Jeff I think walked you through very clearly, will grow mid single digits organically for the year. Fueled by new products, market share gains and a return to growth in our emerging markets. In Security, which has historically been among our higher margin businesses, we expect profitability will improve throughout the year as the Niscayah integration synergies and the benefits of a modified field sales model in North America begin to hit the bottom line, and as a consequence, we expect modest year-over-year improvement. So 2013 will be another solid step towards the achievement of our mid decade vision. With 3% organic growth and 16% to 21% earnings per share expansion. With that, I would like to turn it over to Kate and Lorraine and we will start our Q&A.

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

Great. Thanks, John. Lorraine, let's open up for Q&A.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

David MacGregor, Longbow Research.

David MacGregor - *Longbow Research - Analyst*

Yes, good morning, everyone. John, I wonder if you could just talk about market share trends within the Security business, particularly the Convergent Security business.

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

Sure. Within Convergent Security, we clearly lost a slight bit of share, both in Europe and North America, some of which was programmed. If I start with the US, we've got some good installs. And as Jim suggested in his segment overview, some of those larger jobs came at the expense of margin. But even with that, we arguably have I would say very, very modest share decline in North America, as we attempt to upgrade our mix and integrate the Niscayah business. And we remain highly focused on new vertical markets such as financial services, government, education, but you will recall our largest single market right now, or vertical market, is retail. And of course, that is not a very robust market. So globally, we arguably saw some modest share loss, which we believe is temporary.

Europe as I suggested, our business remains very strong. We remain a market leader. We did suffer some share loss particularly in the Nordic markets in Sweden. A legacy Niscayah strong hold. The rest of the business remains very strong. We remain strong in France. We've lost business in Spain but we've gained share because we've lost business at a far slower rate than the market. And Jim if you want to add anything on to that, please feel free to do so.

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

Yes, I think when you look at the competitors, and their various reports, there is no indication that anything but share loss and share gain at the margin is going on. There is no sweeping trend here. You have the largest competitor in the electronic industry shedding some less profitable business so their numbers are not terribly strong. You have nothing really meaningful going on, underneath the two of us, the largest of us being the second largest, and no real meaningful trends with the other electronic players. Although there is some noise coming out of a few of them, but thus far, nothing to get too excited or concerned about. And mechanical, I would say that I think we're gaining share in the US.

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

Absolutely.

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

And that's a terrific turn of events there. Very recent turn of events. But it is a new business model that we have taken on. Certainly seems to be paying some dividends in the early stages so that is really positive. And then as John mentioned, the European situation, we do have a strong business there and we're very pleased with it. We have been shedding some business intentionally there, and the market is not terribly strong either. I think John covered that very thoroughly.

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

Thanks, next question.

Operator

Dennis McGill, Zelman and Associates.

Dennis McGill - *Zelman & Associates - Analyst*

Yes, thank you, guys. I guess it's kind of a related question but was hoping within the CDIY business if you could maybe break out expectations domestically versus internationally, if you think about it, for the year. Then as it relates to the promotional discussion that you talked about in the first quarter. Any help that you can provide on what that impact was on the margin side, that will be shifted towards 2Q, 3Q.

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

Dennis, this is John. Jeff is going to take all but the very end of your question. We are not going to drill into margins forward looking, by segment or by business. I think we can talk to it arguably directionally, but Jeff why don't you take that.

Jeff Ansell - *Stanley Black & Decker, Inc. - SVP and Group Executive, CDIY*

As we look at the full year, our expectation is that we will have the North American marketplace will perform essentially at the range we provided which is mid single-digit growth, with a plus or minus a point either way but around mid single-digit growth there.

Some pressure in Europe. Volumes are holding up pretty well as they did last year. But that business continues to be somewhat pressured. Offset by strength in the Latin -- or the emerging markets which will grow double-digits. So, if you combine those three things, you have strength in emerging markets, above our mid single-digit total range, you have some pressure in Europe, as expected. And North America will perform about at the range of the total business.

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

And Dennis, just retrospectively to touch on your margin question, as I say, we are just never going to do this prospectively. But we did report strong margins on flat volume and the math would suggest that was due in part to the delayed promotional activity that Jeff talked about but an equal greater proportion to the strong product mix. Outdoor is a terrific business, but it is not among our highest mix businesses. So less outdoor, less promotion, really strong professional power tool performance, certainly helped deliver the very solid margins in the first quarter. Hopefully that will help you, prospectively, we're just not going to go there on this call.

Operator

Mike Wood, Macquarie Capital.

Mike Wood - *Macquarie Research Equities - Analyst*

Hello, thank you. Would you be able to talk about the rate pressures that you saw on CSS, what regions they were in? And also along those lines how Niscayah is tracking versus your expectation from a sales perspective?

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

We will have Don take it. We have touched on that but we will try to elaborate.

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

Mike, as Jim articulated and I touched a little bit on guidance, CSS is definitely seeing a combination of volume and rate pressure. There's certainly volume pressure in Europe, some of which we anticipated and some of which is a little bit above expectations, but the rate pressure is also in Europe because where we're seeing that volume pressure is in the Nordic region, which is the highest profitable business we have in the European CSS business. We believe it is temporary in nature. But it does require us to accelerate some of the cost synergies that we touched on through the call. And we believe that can quickly get us back to a level of profitability that we're comfortable with.

In North America, we have a little bit of rate pressure, as we saw some mix shift from larger install jobs, but that is really us just continuing to focus on the vertical strategy in that business and ensuring that we are achieving the right levels of profitability and we believe that is a temporary phenomena. A lot of that was actually planned for in Q1.

Mike Wood - *Macquarie Research Equities - Analyst*

Thank you.

Operator

Steven Kim, Barclays.

Unidentified Participant - *Barclays Capital - Analyst*

Hello, guys. It is actually John filling in for Steve today. So in the release, once again, you laid out the $15 billion sales target by mid decade. Clearly I would think that acquisitions are a big part of that, or reaching that, and there a few potential targets that are being shopped in the market. So I was wondering if you could talk a bit about how you're evaluating M&A and to what extent future tax planning plays in that analysis?

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

Yes, I will take that. I guess three points. One as we've said, the temporary -- the very publicly announced temporary hiatus in our acquisition program allows us to digest several of the recent acquisitions, particularly Niscayah and Infastech. And focus our efforts both in terms of organizational capacity and to a lesser extent spending on our organic growth initiatives. That is number one. Number two, we hadn't -- we didn't have, three years ago, we didn't have Black & Decker on our M&A or BD target, but the opportunity to combine two phenomenal businesses with even greater synergies presented itself, and as an opportunistic proactive Management team, we seized that opportunity. That is a long way of saying were that to present itself again, it is not saying we won't do it.

Tax planning is a tertiary thought as we look at our M&A and business development plan. Specifically those who have followed us, we have a very careful screening, strategically. Is it one of our four identified growth platforms, and then financially, does it achieve our hurdles, last but not least do we have the organizational capacity to absorb it. All three of those things go into our thinking and our planning. And it will continue as this year progresses.

We haven't in the past nor will we ever talk about specific targets. But this Company, acquisition, valuation and integration, is or is rapidly becoming a recognized core competency in this Company, and we have been given a lot of credit for that. We haven't forgotten how to do it. Long term, it will remain part of our strategy. But temporarily it is on the back burner.

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

And if I could just elaborate as well, we come at M&A more from a strategic point of view than we do trying to fill in some goal that we have for the mid decade. So we're not out there just willy-nilly shopping around so we can get the $15 billion. What we do believe is that with the capital allocation approach that we have and with the revenue growth objectives that we have -- which would be low double-digits total growth, and then 4% to 6% organic, long term objectives, that we can get to something along the lines of $15 billion, by the middle of the decade, using our very publicly stated acquisition strategy.

Which is to continue to consolidate the tool industry, number one. Which means strengthening our CDIY and IAR businesses, through investments in particular. In this particular market, the accessories is the area that we really are underrepresented in, it is the most profitable area in the power tool business and it's one where we are constantly looking for opportunities. These would tend to be bolt-ons in this particular space but we will continue to pursue those.

And then the other area that we're focused on is in emerging markets for the Tool business. Because there is plenty of opportunity to continue to complement our organic growth strategy in Tools with an acquisitive growth strategy. So protect the core through M&A, protect the Tool business, and then we move to the growth platforms. We have four growth platforms, we have Security, Engineered Fastening, Infrastructure, and Healthcare. We'll start with Healthcare, because we're only $170 million in Healthcare today and we're not going to go out and buy a multi-hundred million dollar healthcare business that trades at 4 or 5 times revenue. That is just not what we're going to do. Healthcare, we may do some small technology bolt-ons that could help improve our value proposition where we bring efficiency and safety and security to hospitals.

But the other three areas are the ones that are you likely to see M&A activity in the future. Engineer Fastening, we just completed one so I wouldn't expect anything too soon there. And you have Security and you have Infrastructure. And as you know Security business, those folks are busy digesting Niscayah and also getting their organic growth on track so they probably won't be doing anything significant in the near term. However, as we look further out, I would expect to see some activity in the emerging markets and perhaps some activity targeted at industrial verticals such as retail, financial services, government, et cetera.

And then finally, Infrastructure. And we will continue to see plenty of opportunities in Infrastructure, where we can find niche positions that are in secular growing areas that can be defended that have high margins and high growth associated with them. So we would probably see some activity in that area on a prospective basis. But as we said last July, 12 to 18 months hiatus. We're coming up on July, we have made some good progress, but we will not continue an acquisition strategy above and beyond emerging markets until we get to the point where we can say definitively that the organic growth initiatives are working.

Operator

Eric Bosshard, Cleveland Research.

Eric Bosshard - *Cleveland Research Company - Analyst*

Good morning. Curious, I see the investment and the discussion on organic growth across the business. I'm curious how you're balancing this thinking in the Security business, trying to grow Security, improve organic growth share there while at the same time you are taking costs out. So, if you could talk a little bit about how you're balancing the spending there and especially thinking about Niscayah with the market share and the growth objectives.

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

I think it is fairly simple. I think when you look at the model, Eric, the North American business, we are investing for growth right now. And the European business, we are right-sizing the cost structure to reflect the revenue reality. So that's where you see the cost out, the synergy increases is all in Europe and in North American we're investing significantly in vertical markets, in particular the vertical market growth strategy. And it's as simple as that. It is a bifurcated approach.

Eric Bosshard - *Cleveland Research Company - Analyst*

If I could just follow up, the assumption for the year sounds like you expect to make up the margin short fall in that business through the rest of the year. What changes in 2Q to 4Q relative to 1Q especially in light of the investments you're making?

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

I think I will take it, Jim can elaborate if he would like. I touched on that in my comments and I will try to clarify. Two things. Obviously, Niscayah increased synergies in and of themselves will make up mathematically for some of the volume shortfall and some of the margin shortfall, again, the Niscayah synergies, they get greater every quarter -- the run rate, not smaller. Second, Jim alluded to it in his segment discussion. We have modified our, if you will, go to market approach via distribution, in North America, on the Mechanical side of the business, and early signs are it has been tremendously successful. And we think that is going to continue.

A lot of other moving parts, and Don talked about the total Company. Within Security, Brett would talk about a lot of puts and calls that are neutral. But strong Mechanical Security business, as well as Access business, getting stronger, and continuing to put a lot of points on the board from Niscayah cost synergies, we do believe will get us back to where we've been. And Eric, you've followed this business a long time, it historically has been a very profitable business, and the math with Niscayah was low -- very low single-digit operating margin when we acquired it. It is double-digit operating margin. And it is going to get to fleet average within a year or so and that is just a really big piece of it.

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

I know that when we talk about investments in verticals, it sounds kind of generic and it doesn't really have a lot of life to it. But when you start talking about the individual verticals and what we can bring to -- what we can and are bringing to the market right now, it is very obvious that we have solutions that are differentiated in a number of these verticals. Just take K through 12 for example. Where we have the full array of Mechanical, Electro Mechanical and Electronic solutions to bring to a K through 12 scenario. And every school board in the United States is evaluating their security right now. We have deployed an army of people around that opportunity. That will come to fruition at some point in time. We are the best positioned security company in America to deal with that opportunity.

In Financial Services, we have the best iris identification technology in the world -- exclusive rights to the best iris identification technology. We are in discussions with major financial institutions about how we help them create branches that are keyless branches using iris identification technology. At some point, that will likely come to fruition. And I could go on and on, in retail what we are doing in retail, what we're doing with government, what we are doing with the RTLS technology that we acquired from AeroScout. But if you start to really delve into these solutions, our opportunity at this point is to commercialize them and that's what the Security people are focused on and that's why we're investing in North American Security.

And oh, by the way, once we get these solutions nailed down in North America, the next wave after that is going to be take them to Europe. So right now we are getting Europe right-sized so it is profitable, robust and we have a strong management team in place which we are well on our way to doing. And then a year or two from now there will be a wave of solutions, these same solutions, coming in to Europe. And then finally, we're investing in the emerging markets in Security. Our business this year will be about $100 million, in Security in the emerging markets.

The Tong Lung acquisition, which was quietly done, and the GMT acquisition, which was done several years ago, have really provided us with outstanding manufacturing and design capability. We recently completed a series of [Ion] products, which are the European type standard products that play much more successfully into the emerging markets. Now we have Chinese manufacturing capability. We have Taiwan design capability. And all of that is being assembled for a frontal attack on several of the major emerging markets. So growth in Security is coming. And investments are being made. And it is an exciting time I think for the Security business. But we're at the threshold of it at this point.

Operator

Jeremy [Kaprin], CLSA.

Jeremy Kaprin - *CLSA - Analyst*

Good morning. Thanks. Just a question on the hand tools business. You talked about strong performance of the new DeWalt line. So I wonder what is that is actually holding it back over the past couple of quarters, and if you had any comments on market share around this?

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

Yes, certainly. Jeremy, as indicated, the power tool brand usage in our hand tool business has really been positive. While the core Stanley business remains very strong globally. The challenge, and from a share perspective, we believe our share has increased in hand tools over the past three years. So from a share perspective, quite positive, introduction of power tool brands, our power tool brands in hand tools have been predominantly incremental.

The pressure that business has faced in the past quarter, and probably past couple of quarters, is high exposures, relatively high exposure to Europe, which is a strong hand tool market for us, that really has been pressured like -- in that business like every other. So that really has offset some of the growth we've had from the power tool brand perspective in our hand tool business. But we continue to make progress from a share perspective. And we expect too that business will grow consistent with the rest of the business as guided already, for the remainder of 2013.

Operator

Liam Burke, Janney.

Liam Burke - *Janney Capital Markets - Analyst*

Yes, thank you. Good morning. You highlighted margin synergies, and with a few exceptions you seem to be on track both from a revenue and margin side. CapEx is roughly in line in the 2.5% to 3%. Are you comfortable that you are making the progress you need to meet your ROCE target of 15% -- or objective of 15%?

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

This is Don. I would say yes, we are comfortable. I think we had mentioned I believe back in January that one of the -- if you want to call it a benefit of us taking this temporary tactical pause around M&A, is it allows us to focus on enhancing our return on capital employed. What you have seen over the last five years in particular, and even before that. As we did acquisitions that, before they get integrated into our existing core businesses, they have a lower return, and they get to the range of 12% to 15% return on capital deployed by somewhere between year three through five, post-acquisition.

That has been a bit of a -- if you want to call it drag on that overall return to the Company. But still, the return to the Company has been around 10% in that time frame. Which is certainly significantly above our cost to capital. But we want it to be closer to 15% as you mentioned by the middle of this decade. This pause allows us to make a lot of progress. We think we can make about 100 to 150 basis point improvement this year. The other great benefit of the organic growth initiatives over the next three years is minimal investment to make that happen. And a return of $200 million of operating margin by year three really does -- gives us a dramatic boost on those returns as well.

Operator

Peter Lisnic, Robert Baird.

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

Good morning, everyone. Just on the positive trends you noted on the business model shift, that Mechanical Access. You can give us a little flavor as to how that translates into maybe a margin progression this year, but more importantly what that means longer term for the business from a return perspective and potentially does it enhance the growth aspects of the platform as well? Thank you.

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

Yes, Pete, I will say for the third time this morning, we are not going to project margins by sub segment of business going forward. It does us no good. And we don't -- we're not sure it helps you that much. I understand the desire from a modeling perspective. What we can say -- and I think Jim articulated this quite well, we were slow to shift our model because we had something that was working, but it absolutely will be a catalyst for more organic growth in the North American Mechanical Security market.

We were missing a lot of opportunity in terms of both specification and with mid price point products, with our purely direct model which served the high end extremely well, and restocking captive customers extremely well. But it left us a little void in a lot of areas where we felt it was absolutely essential, we have greater penetration to grow the market. So at the end of the day, a better mid price -- a mid price point product offering, broader distribution, will absolutely be a stimulus for organic growth, and we would not do it if we didn't think it was going to be incremental or positive vis-a-vis margins but we're certainly not going to forecast that for one small segment of one segment of our business.

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

It is an interesting time, when you look at what is going on in distribution and Mechanical Security, because these distributor, as they went through tough times, they doubled down on growth and driving organic growth themselves. And really started pushing the envelope up into the Electro Mechanical and even into Electronic in some cases. So our business model plays very nicely into that trend.

And then second thing I would say is while we were farming our installed base very effectively, the armies of distributors that are out there that are hunting in the commercial construction area are absolutely winning that war. And so therefore, if you don't play in that arena, with them, you don't get the opportunity to participate in the commercial construction growth that is ahead of us. And so there are several other reasons for doing what we did, but those are two good ones.

Operator

Jeffrey Kessler, Imperial Capital.

Jeffrey Kessler - *Imperial Capital - Analyst*

Thank you. And speaking of Mechanical Security, at the ISC show, you demonstrated what may not be your first -- but it was certainly the first that I saw demonstrated, integrated a network mechanical door that would be networked with CSS. Can you speak a little bit about the -- if you want to call it the convergence of getting your Mechanical and your Electronic businesses together, particularly at the door?

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

Yes, I mean that is definitely a thrust of ours. You saw the product. That is going to be first --

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Jeffrey Kessler - *Imperial Capital - Analyst*

I think it was the ES8 or the EL8 or something like that.

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

It is called the EL.

Jeffrey Kessler - *Imperial Capital - Analyst*

Okay.

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

The EL Lock. Which will be introduced en masse in May to the marketplace and was spotlighted at the show, and it will be at a price point that no one else can even get near. And that is with source manufacturing to begin with. That can be brought in house if we so desire at some point. That is a key part of our strategy, it certainly plays to many of the verticals that we're looking at.

It also gives us quite an edge with respect to what I was just talking about with the independent distributors and the fact that they are moving into the Electro Mechanical and the Electronic realm. And that comes in both a network and a non-networked version. And we're expecting pretty good -- big things. I didn't really talk about that as a part of the equation for Mechanical Security growth as we go forward, but that is certainly out there as something that can help drive it.

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

Great. Well I think that wraps us up, Lorraine, correct?

Operator

That is correct. I am showing no further questions.

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

Well, thank you all so much for dialing in today. If you have any questions, please just send me an e-mail or give me a call and I will talk to you all soon. Thank you.

Operator

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