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SWK - Q1 2017 Stanley Black & Decker Inc Earnings Call

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OVERVIEW:

Co. reported 1Q17 revenue of $2.8b and diluted adjusted EPS of $1.29. Expects 2017 GAAP EPS to be $7.95-8.15 and adjusted EPS to be $7.08-7.28.

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PRESENTATION

Operator

Welcome to the Q1 2017 Stanley Black & Decker, Inc. Earnings Conference Call. My name is Chelsea, and I will be your operator for today's call. (Operator Instructions) Please note that this conference is being recorded.

I will now turn the call over to the Vice President of Investor Relations, Greg Waybright. Mr. Waybright, you may begin.

Gregory Waybright - *Stanley Black & Decker, Inc. - VP of IR*

Thank you, Chelsea. Good morning, everyone, and thanks for joining us for Stanley Black & Decker's First Quarter 2017 Earnings Conference Call. On the call, in addition to myself, is Jim Loree, our President and CEO; Don Allan, our Executive Vice President and CFO; and Jeff Ansell, our Executive Vice President and President of our Global Tools & Storage business.

Our earnings release which was issued earlier this morning and a supplemental presentation which we will refer to during the call are available on the IR section of our website as well as on our iPhone and iPad app. A replay of this morning's call will also be available beginning at 2:00 p.m. today. The replay number and the access code are in the press release.

This morning, Jim and Don will review our first quarter 2017 results and various other matters, followed by a Q&A session. (Operator Instructions)

As we normally do, we will be making some forward-looking statements during 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's therefore possible that actual results may materially differ 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 filing.

I'll now turn the call over to our President and CEO, Jim Loree. Jim?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Thanks, Greg, and good morning, everyone. As you saw, the first quarter was an excellent start to 2017. All our businesses came out of the gate strong, with each contributing to our robust 5% organic growth for the quarter.

Revenues were $2.8 billion, up 5% versus prior year on strong organic growth. Tools & Storage continued to lead the way, up 6% in the quarter, with all regions contributing. Industrial posted a large positive top line surprise with 4% organic growth on strong automotive system sales in Engineered Fastening and solid performance from the infrastructure businesses, which are finally beginning to see signs of life in their various end markets. This is an 8 point positive sequential swing for the segment. And while it's still too early to conclude definitively, we're cautiously optimistic that we may begin to see the positive trend continue as the year progresses. Don will provide some more color on that when he goes through the segment details and our updated 2017 outlook in a few minutes. Finally, our Security business started the year off right, posting 1% organic growth, in line with our expectations.

It was good to see the top line expansion driving impressive operating leverage throughout the P&L, expanding our operating margin rate by 110 basis points to a record first quarter rate of 14.2%, excluding M&A related charges. This reflects our consistent focus on operational excellence as evidenced by a 160 basis point increase in our gross margin rate, overcoming an adverse impact from currency and some commodity inflation.

Diluted adjusted EPS for the quarter was $1.29 as strong operating performance more than offset the aforementioned currency and commodity headwinds, higher restructuring charges as well as an unplanned event-based environmental charge related to a premerger closed facility. On top of these excellent financial results, we also closed 3 major capital allocation transactions in the quarter: finalizing our acquisition of Newell Tools, our acquisition of the Craftsman brand as well as the divestiture of our commercial hardware business, which I'll address in more detail in just a moment.

Finally, based on the strong start and our improved outlook for the Industrial businesses, we are raising our 2017 full year adjusted EPS guidance by $0.10 to $7.08 to $7.28. This is inclusive of the previously disclosed impact of the 3 transactions I just mentioned and will be covered by Don later during his remarks.

Turning to our recent portfolio activity. In what made for a very busy quarter here, the Newell Tools acquisition with the iconic Lenox and Irwin brands closed on March 10, the day after the Craftsman deal closed. As you would expect, our experienced integration teams are up and running full speed on the Newell integration and building out the Craftsman brand.

On Craftsman, the majority of our efforts have focused -- are now focused on supply chain activities to initially support sales into non-Sears Holding channels. In parallel, we are developing commercial strategies for the brand and remain very excited about the potential growth opportunities. We continue to see a clear path towards annual growth of approximately $100 million a year for the next decade.

Our initial conviction has only been reaffirmed since closing as numerous customer interactions continue to substantiate our growth assumptions. This is reinforced by the powerful name recognition and consumer buying intent associated with the Craftsman brand. Suppliers are also positive about the opportunity to participate in reinvigorating the growth of this iconic brand.

As expected, there's a lot of excitement and positive energy around our stated intention of bringing manufacturing for the Craftsman brand back to the United States. Our plans for a new state-of-the-art manufacturing facility are starting to take shape, so look for more to come on this front in the coming quarters. And as previously communicated, we expect the Craftsman brand transaction to generate approximately $0.08 of earnings accretion in 2017, excluding charges, building to $0.35 to $0.45 accretion by year 5.

On Newell Tools, our focus is now on integrating employees, suppliers and customers into our existing operations. The team is focused on achieving the substantial cost synergies identified during due diligence. And as a reminder, we expect to achieve $80 million to $90 million in cost synergies with this deal, and we'll also soon begin tapping into the significant revenue synergy opportunities.

Overall, customer feedback has been extremely positive, with many customers voicing a desire to expand their relationship and add new product lines. Work is well underway to accommodate these expansions, including new distribution channels for the Lenox and Irwin brands into previously underserved markets where Stanley Black & Decker has a strong and established footprint.

We continue to expect Newell Tools earnings accretion of approximately $0.24 per share in 2017, excluding charges, building to approximately $0.80 by year 5. So as you can tell, we are excited about the prospects for these acquisitions, both for the strategic benefits as well as their financial impact.

Regarding the total company, we believe we are set up well for a strong 2017. As always, we benefit from our deep and agile leadership team, our commitment to and focus on operational execution and our robust SFS 2.0 operating system. We're also benefiting from relatively stable exchange rates. And for the first time in 4 years, we are not facing escalating FX headwinds at this stage of the year. The result is a healthy start to 2017 with a focus on maintaining the momentum behind our organic growth and margin expansion efforts while also tapping into the significant value opportunities presented by Newell Tools and the Craftsman brand acquisitions.

I'll now turn it over to Don for a more detailed discussion of first quarter results. Don?

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Thank you, Jim, and good morning, everyone. I would like to take a deeper dive into our business segments, which all performed very well in the first quarter.

Tools & Storage revenue was up 9% in the quarter as 6% organic growth and 4 points of acquisitive growth were offset by 1 point of currency pressure. The operating margin for this segment was up an impressive 16% year-over-year to a 16.4% operating margin as the group achieved strong operating leverage and had solid top line growth.

Each Tools & Storage region and SBU posted positive organic growth in the quarter. On a geographic basis, North America led the way and was up 8%. This strong performance was due to our U.S. commercial and retail channels, which were up low double digits and high single digits, respectively. Additionally, Canada posted solid organic growth of around 10%.

New product introductions and successful field conversions drove growth in the commercial channel. Strong e-commerce volumes and continued momentum from the FLEXVOLT launch fueled growth in the U.S. retail channel as we did overcome some modest channel inventory tightening.

We expect the momentum surrounding FLEXVOLT, which, by the way, did meet expectations for the quarter, will be maintained and bolstered by our commercial team's launch strategy, which has a well-designed road map of promotions and new FLEXVOLT tool and accessory SKUs hitting the shelves regularly over the next few years. North American POS data remained healthy throughout the quarter as it was up high single digits. This is particularly impressive given we were comping a mid-teen POS growth rate in the first quarter of 2016.

The above-market growth trend in Europe continued in the quarter, with the region posting 6% organic growth. The outperformance was widespread across the region, with almost all markets contributing. The European team continues to provide picture-perfect examples of commercial excellence at its finest, driving mid-teens growth on average among its top 10 customers in the quarter. Additionally, in the first quarter, we continued to see customer wins in the U.K. and strong market share gains in Italy and Iberia.

Finally, the emerging markets were up 1% organically as solid performances in Latin America and Asia were weighed down by continuing but improving pressure in the Middle East and North Africa. We are undergoing a transition to a direct model in Turkey, which will weigh on growth within that region for the first few quarters but should ultimately provide a much better mid- to long-run opportunity in that country.

Performance in Latin America was mixed, with double-digit growth in Mexico, Brazil and Ecuador more than offsetting declines in Colombia and Argentina. Asia delivered strong performances in Korea and Japan, which more than offset pressure we saw in Thailand and in the Philippines. The diligent pricing actions that we've been taking as well as the ongoing MPP launch across the developing markets is continuing to drive growth.

Just one last comment on emerging markets. We are really beginning to see a lot of excitement from our customers around the potential future Irwin and Lenox rollout. More to come on that later this year.

Within the SBUs, all lines were positive in the quarter. The power tools and equipment group was up 9%, led by power tools and home products, both of which benefited from new product rollouts and continued strong commercial execution. Our hand tools, accessories and storage organization delivered 3% growth on a strong performance within hand tools and storage, which benefited from a bounce back in industrial end markets.

The overall Industrial businesses within Tools & Storage were up mid-single digit. In total, the Tools & Storage organization continued its momentum in the first quarter, delivering solid above-market organic growth and robust operating leverage, driving a 110 basis point margin expansion while, at the same time, accelerating integration and commercialization efforts around the Newell Tools and Craftsman brand acquisitions.

Let's move to Security. The Security segment had a nice start to the year as well, coming in right on top of our expectations, posting 1% organic growth. North America organic growth was up 2%, its highest organic growth quarter since the second quarter of 2015, led by higher volumes within automatic doors, which continues to perform very well, as well as solid health care growth. Europe was flat organically in the quarter, with mixed results across the markets as gains in the Nordics and U.K. were offset by declines in France and Central Europe.

In terms of profitability, the segment contracted 120 basis points year-over-year but was relatively in line with our expectations. The sale of the mechanical locks business, which was finalized in the quarter, drove approximately 70 basis points of that contraction as this was an above line average business. The rest of the operating margin rate decline is a combination of channel mix and strategic investments within the sales organizations of Europe and North America.

On the whole, the Security segment delivered a solid quarter, starting the year on the right foot from an organic growth perspective; at the same time, executing seamlessly on the mechanical locks divestiture. Additionally, they had a strong orders trend in the quarter, and therefore, backlog is positioned well going into the second quarter.

Now turning to Industrial. We are extremely pleased with the segment's outperformance this quarter as both the Engineered Fastening and infrastructure businesses delivered positive organic growth in excess of expectations. This top line performance generated significant operating leverage and drove 180 basis point improvement in operating margin rate for this segment as volume, productivity and cost actions more than offset currency headwinds.

Engineered Fastening delivered 4% organic growth on a strong performance from the automotive business, up low double digits, which more than offset lower electronic volumes which were down 20% for the quarter. Auto fastener sales continued to outpace light vehicle production numbers globally by a ratio of about 2:1. Additionally, auto system sales were also a highlight in the quarter, up significantly versus the prior year on the back of previously won business beginning to translate into new model production. The Engineered Fastening team posted a record operating margin rate in the quarter, in the low 20s, as top line growth combined with recent cost-out actions delivered significant operating leverage.

The infrastructure businesses posted a solid quarter as well in their own right, up 2% organically. Our Hydraulic Tools business, which has been revamping its commercial execution and go-to-market strategies for the last year or so, is starting to see some momentum build, posting its second consecutive quarter of organic growth due to higher volumes across all regions. Meanwhile, oil and gas was flat in the quarter but also ahead of expectations as this industry begins to experience accelerated onshore pipeline construction activity within North America. However, this is being offset by a continued low offshore project activity factor.

While there is still a lot of risk and uncertainty in our operating environment today, both geopolitically and economically, we are very encouraged by the collective performances across the portfolio in Q1. As we move deeper into 2017, we will remain focused on driving outsized organic growth and operating leverage while also integrating the Newell Tools and Craftsman acquisitions into our world-class Tools & Storage franchise.

Now let's briefly take a look at the quarter's free cash flow performance on the next page. We were down slightly year-over-year, mainly attributable to higher working capital as the large swings in net income and other were primarily driven by the gain on the Mechanical Security divestiture. As a reminder, the outflow of cash in the first quarter is normal seasonality, where our Tools & Storage inventory levels rise to ensure we are adequately prepared for the Q2 and Q3 demands of our key customers in the developed markets.

However, keep in mind working capital turns in the quarter were up 0.9 turns versus the prior year when you exclude the impact of the portfolio move, a very solid start to the year. We remain on track to deliver 100% free cash flow conversion for the full year. Just a reminder, this guidance is excluding the impact of the gains on the recent divestitures.

Now let's turn to our 2017 guidance. As Jim mentioned earlier, we are raising our adjusted EPS outlook for 2017 to a range of $7.08 to $7.28, which is an increase of 9% to 12% versus the prior year. On a GAAP basis, this results in a range of $7.95 to $8.15 earnings per share, inclusive of various onetime charges and also the gains from the first quarter divestitures I previously mentioned. This $0.10 increase to our outlook comes through as a combination of slightly higher organic growth within our industrial-related businesses, which contributes approximately $0.08; and incremental cost and productivity actions of $0.10, primarily within Tools & Storage. In the aggregate, this more than offsets the previously mentioned onetime first quarter environmental charge of $0.08.

Additionally, we are maintaining our combined FX and commodity inflation headwind estimate at $100 million to $105 million. Additionally, we still expect $50 million of core restructuring for the year. However, keep in mind, that $50 million is inclusive of the $12.5 million charge we took in the first quarter relating to the settlement of a legacy Canadian defined benefit plan. Finally note that we expect second quarter EPS to be approximately 27% of the full year 2017 guide.

Turning to the segment outlook on the right side of the page. Organic growth within Tools & Storage is still expected to be mid-single digits as healthy construction markets in the U.S. combined with a relatively stable Europe and a still volatile emerging market setup should allow us to continue to take share around the world. That top line growth will translate into improved margin rate year-over-year.

We are maintaining the organic growth view on Security as well, up low-single digits in 2017. Note that the margin rate for this segment will be down year-over-year as we begin the process of lapping comps inclusive of the mechanical locks business just divested this quarter. Excluding that sale, however, the margin rate for the year will be flat to slightly positive.

Finally, we are raising the top line outlook for our Industrial segment from previously down low single digits to now relatively flat. It's still a little too early in the year to make any more aggressive predictions in this space, but we are seeing some positive signs both in the Engineered Fastening end markets as well as within the infrastructure businesses. We continue to see operating margin improvements in this segment, driven by the previous identified cost actions but also due to the improved revenue outlook.

As I noted before, there is still quite a bit of macroeconomic and geopolitical uncertainty across our operating landscape in 2017. However, we remain cautiously optimistic as we are seeing signs of growth across all segments of the business in the first quarter, and we believe we have a solid path to delivering the full year revised guidance and outperforming the broader market from an organic growth and margin expansion perspective once again. We will remain focused and disciplined in our pursuit of that goal, particularly as we integrate and begin building momentum within our newly acquired tools businesses.

With that, I'll turn it back over to Jim to summarize this morning's call.

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Thank you, Don. Well, as you've heard, Stanley Black & Decker is hitting on all cylinders. The first quarter represented a solid start to the year as we continue to build on the momentum underlying our organic growth and margin expansion initiatives. As a result of this strong operating performance and a reasonably favorable operating environment, we raised guidance excluding charges and the gain on sale of the Mechanical Security business to $7.18 at the midpoint, a 10% increase on a year-over-year basis.

Apart from our focus on organic growth, we're very excited about the opportunities to drive value within the Newell Tools and Craftsman brand acquisitions. And as I mentioned earlier, integration activity is well underway for both transactions, and we've received nothing but positive feedback from all constituencies.

And finally, I want to remind everyone that we will be hosting an Investor Day in the morning of May 16 in New York City. This will be a great opportunity to communicate our strategic and financial objectives and discuss the next chapter in the company's evolution. We're also looking forward to showcasing members of our business unit and other key functional teams, and we look forward to seeing you there.

We're now ready for Q&A. Greg?

Gregory Waybright - *Stanley Black & Decker, Inc. - VP of IR*

Great. Thanks, Jim. Chelsea, we can now open the call to Q&A, please. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Chris Belfiore with UBS is online with a question.

Christopher Belfiore - *UBS Investment Bank, Research Division - Equity Research Associate Analyst of Industrials*

So I guess I just wanted to kind of touch a little bit on the strength you guys saw on Industrial -- in the Industrial segment, so the engineering -- the Engineered Fastening business with the automotive systems performance there. Is this something that can kind of be lumpy through the year? Just kind of -- I know you said you're kind of looking to see how things are going to play out, and that's why the organic growth is still at relatively flat for the year. But I mean, that would then kind of imply that it could be maybe more first half weighted than second half weighted just getting to like the annual guidance there. So is it kind of a lumpy thing? Or is it specific to like a project?

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Sure. This is Don. It is somewhat lumpy in the year, where we do have -- like we experienced in the first quarter, we'll probably have a similar dynamic in the second quarter around system sales within Engineered Fastening. But in the back half, right now, we really don't see a lot of those types of system sales occurring as a lot of the new model launches are happening here in the first half of the year. The back half of the year right now, that's not the case. So that's part of the reason that we're being a bit more prudent and balanced in our view of the full year for that particular business. Those dynamics can change a little bit every once in a while, but at this stage, we think that's the most appropriate perspective of the full year.

Operator

Rich Kwas from Wells Fargo Securities is online with a question.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD and Senior Equity Research Analyst*

Two questions. One, I guess, Don, just a follow-up on the Industrial question. From a mix standpoint, what are you assuming for auto for the back half of the year? When we look at it from a production standpoint, there is some concern, North America and maybe even China, that things slow down. And then just a broader question for Jim around the manufacturing facility for Craftsman. How are you looking about the expansion into the U.S. with the new facility given that there seems to be increasing certainty regarding the BAT and that sort of impact on your manufacturing position? Are you -- how committed to you are it -- are you committed to it, I should say? And then any implications from anything that doesn't go on tax-wise?

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Okay. I'll start with the first question, Rich, and continuation of the previous question, which -- on the automotive business of Engineered Fastening, we do see really some strong growth here in the first half of the year, just like we experienced in the first quarter. But right now, we do see light vehicle production slowing in the back half, in particular in North America, but even slowing in some of the other regions compared to what we expect to experience in the first half. So that's part -- that is really what's kind of factored into our guidance when we look at first half versus second half in the Industrial business in particular. So you have a combination of the auto system sales and then you have a secondary factor of just a slowing of production in the back half of the year versus the first half based on current projections.

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Okay. And then on the second question, and just to reiterate how committed are we to our U.S.A. manufacturing strategy related to Craftsman given the uncertainty but, certainly, the lower probability of the implementation of border adjustability tax. And frankly, I would just comment on that, that it's good to see that the government seems to be coming around on that one and understanding that, that is not a good idea for the United States of America and many, many companies within the United States as well and really pretty much everywhere. So setting that aside for a minute. As it relates to the facility expansion plans, it was never contingent on a BAT being implemented. It was really a function of the strategy for re-Americanizing Craftsman. And just so everyone's aware, we manufacture about 30% of all tools that we sell in the United States of America today, and we are able to cost-effectively do that with today's manufacturing technology. And our intent is to increase that for the total tools business, including Craftsman but in particular Craftsman. We have 11 tools plants in the United States, and those tools plants, probably the majority of them will be expanding capacity in addition to the facility that we've discussed. And in the end, it may be more than one facility in the U.S. We'll have to see how it all shakes up, but we're looking at various scenarios. So to answer your question, we're very committed to manufacturing in the U.S. for Craftsman and for the rest of our United States sales.

Operator

Saliq Khan from Imperial Capital is online with a question.

Saliq Jamil Khan - *Imperial Capital, LLC, Research Division - VP in the Institutional Research Group*

With the increasing strength in your Tools & Storage market, what are you hearing right now from your distributors and your channel partners about the state of your product offerings? But also, have you been able to conduct a review of the talent as well as the temperament of all the employees within the recent acquisitions?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Would you repeat the first part of your question, please?

Saliq Jamil Khan - *Imperial Capital, LLC, Research Division - VP in the Institutional Research Group*

Sure. If you take a look at the strength that you have within the Tools & Storage business, what have you been hearing from the distributors and the channel partners about the state of your product offerings?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Okay. We're going to have Jeff Ansell tackle that one since he's right on the job.

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

Thank you. To this point, the response that we've received from both end users and trade customers globally have been -- has been outstanding. Day 1 favorability on the Craftsman news was 90%. From an Irwin/Lenox or a Newell Tools perspective, similarly positive feedback from customers and employees. So day 1, we onboarded 3,200 employees to our system seamlessly, and we spoke with over 1,000 customers in the first 48 hours of the integration. And the feedback has universally been great brands, great opportunities. They have struggled pre acquisition. Newell Tools, they struggled to serve their customers in terms of availability of product, service levels. And that's the #1 thing that customers have said to us, get that right and we can grow this business. And I'm pleased to say that in the first -- less than the first month of ownership, we've improved that backlog position, reduced it by over 70%. So we met the #1 objective of the customer. So the feedback from our customers has been outstanding globally and from employees as well, and we think it really strengthens our portfolio and opportunities to serve our customers unlike anyone in the world.

Operator

Jim Ritchie (sic) [Joe Ritchie] from Goldman Sachs is online with a question.

Evelyn Chow - *Goldman Sachs Group Inc., Research Division - Research Analyst*

This is actually Evelyn Chow on for Joe Ritchie. I was hoping you could just give us an update on your gross margin performance, which has been incredibly strong not just this quarter but really for the past 4. Is there anything kind of significant happening either in your internal actions, mix? Maybe just any other items that are kind of driving that kind of year-over-year expansion.

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Sure. I'll take that. Well, there's nothing unusual. I think it's a continuation of all the things that we do under the SFS 2.0 operating system model, which is focused on appropriate pricing actions, driving cost productivity, transforming our back office, et cetera, et cetera, all those different things, commercial excellence, where we're really trying to make sure that we're providing new products at the right price points to gain market share. All that -- that entire operating model is really what drives that on an ongoing basis. So when I look at the first quarter in particular, you've got that dynamic of just continued trend of trying to drive operating leverage as we grow. And so the way that we drive operating leverage as we grow is that we look at various things that I just described, but then we also try to reinvest along -- a portion of that along the way so we can continue to stimulate future growth. And so we don't necessarily let all the leverage drop through, but we let a large part of it drop through along the way. And the only way you're going to get operating leverage is to do the things that I just described, which is focused on pricing, posting -- focused on cost reduction, driving productivity to the supply chain, offsetting inflation that you're experiencing, et cetera, et cetera. So you combine that with the factor that this is the first year we don't have $200 million of currency pressure. We have a number that's 50-ish roughly on an annual basis at this point. All those factors combined with that are resulting in a continued trend of strong gross margin.

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

And Jeff, why don't you tackle that same question and give them a little insight into how you think about it in the tools business as well?

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

Sure, Jim. Thank you. Inside of tools, if you look at last year's period -- this time last year, we had grown about 8%. This quarter, in the emerged markets, we grew another 7%, and we totaled 6%. And as you know, tool P&Ls volume -- are very volume dependent. So with that volume growth, it's given us a lot of degrees of freedom inside of our supply chain. It's driven great productivity while, at the same time, tremendous quality improvements, lowering our warranty return rates. And that -- the volume growth that we have had has been profitable growth, meaning we targeted specific promotional opportunities in specific categories, seasonally adjusted for the right retail environment around the world, and we've been successful. And in addition to that, we fought around the world with all this currency pressure we've faced now for 4 years, to be very, very frontal facing there. And if you look at places like the U.K., we grew 16% this quarter, 8% was volume, 8% was price, given what's going on there. And so if you take all those things into account, we better served our customers and, at the same time, been more reliable and more profitable while we've grown the business at unprecedented levels.

Operator

Tim Wojs from Baird is online with a question.

Timothy Ronald Wojs - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Just on -- I was hoping you could elaborate a little bit on the discussions that you're having with customers just around Craftsman and the distribution strategy there now that you guys own that asset, maybe where the most interest is and just how do you leverage the entire Stanley Black & Decker portfolio to really benefit -- kind of drive the maximum benefit for the total company.

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Jeff?

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

Sure, I'll take that. So it's really too early to declare the commercial strategy. We are -- that's not to say we're not working on it. We're working on it feverishly, and we have been since March 9. But what we could tell you, early read from this process, is we have an incredible demand for the Craftsman product across our U.S. customer base, even in some other international geographies like the U.K. and Australia, but, in particular, in the U.S. In terms of its opportunity within our stable of brands, if you look at our absolute share today, although we are #1 by all accounts and growing faster than the market, we still only -- we own about 20% of the total global market, so 80% of it is still out there for us to go after across 10 or 11 different marquee brands. And if you look at Craftsman in particular, it still represents nearly a couple of billion dollars in the marketplace today. And while we've grown our tool business from $600 million to over $8 billion, that Craftsman franchise has survived, and that tells you what a loyal installed base that is. The customer, however, says that they'd much prefer to find that brand in a lot of other more convenient locations. So our opportunity to take an installed base we've been able to dislodge and make it available across other geo -- other retail options is exactly what the customer is asking for. We'll give a little more clarity May 16, but not full. We are working feverishly on this. And as soon as we are able, we will tell you more about it, but we can't wait to get started.

Operator

Michael Rehaut from JPMorgan is online with a question.

Michael Jason Rehaut - *JP Morgan Chase & Co, Research Division - Senior Analyst*

A couple of questions, if I could squeeze them in. First, if you could give any update on the M&A landscape, particularly in terms of what you're seeing from a pricing standpoint, what people are asking and if you still see valuations reasonable. And should we think about timing that 2017 in perhaps some of your other segments are something that's possible or you're going to be focusing mostly on Tools & Storage? And then just secondly, on the breakthrough innovation front, any updates there as you look at your other segments augmenting what you've done so far in FLEXVOLT?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

Mike, first of all, on the M&A landscape, we just spent $3 billion or almost $3 billion and are integrating feverishly, as Jeff says, 2 major acquisitions in tools. So this is going to be a year of digestion for the most part. And I think everybody should understand and can understand why that would be both from a financial balance sheet point of view as well as an operational bandwidth point of view. So having said that, I would say that pipeline for M&A is about as robust as we've ever seen it, with valuations, in a zone that I think is manageable, with good synergies; not cheap by any stretch, but some really interesting strategic assets out there that are of a decent size, decent enough to move the needle. So we're combing through those right now and doing a lot of analysis and thinking strategically about what makes the most sense. We may do some very small acquisitions yet this year, but there won't be anything which I would call material in size. But be on the lookout in -- as we get into next year for something, in all likelihood, in one of the other segments other than tools. Wouldn't rule tools out, but I would say that in all likelihood, it would probably be in either Industrial or Security, which is where we see the action today. So that's the M&A picture. We can talk more about that at the Analyst Meeting, for people that are interested. As far as breakthrough innovation, I have never been more excited about the opportunities that we see across the company. And we have about 10 teams up and running. We have -- every business in the company has at least one team, and our emerging markets group has a team. And we're all using -- all those teams are using the same formula that we used for the FLEXVOLT under the global Tools & Storage model that we have identified as part of SFS 2.0. So you'll see more information about that at the Analyst Meeting. But I can tell you that we don't expect a 100% batting average on these. But I would think that, if we have 10 teams up and running and have been up and running now for anywhere between 1.5 years to 6 months, in that time frame, there will be some innovations coming out of those teams. We've already seen some. One of the challenges for us will be some of those require commercialization in places or in ways or channels that we don't necessarily have access to today. So another -- one of our challenges related to breakthrough innovation will be getting some channel access to -- for some of these innovations that are a little bit out of the fairway, if you will. And I think you're going to see a combination of human resources additions to tackle those challenges, as well as some integration of M&A activities with our breakthrough innovation activities and synergizing off both of those. So really exciting times here at Stanley Black & Decker as far as breakthrough innovation goes.

Operator

Dennis McGill from Zelman & Associates is online with a question.

Dennis Patrick McGill - *Zelman & Associates LLC - Director of Research and Principal*

Don, I was hoping you can maybe expand a little bit on the first quarter margin within Tools & Storage. I think we went into the quarter expecting both currency and brand investment to be some pressure on margin and very strong margin performance there. So a little color there. And then as you look at the full year, the positive year-to-year, some different factors going on, especially with the acquisitions. Specific to Craftsman, can you just maybe put some numbers around it given the royalty payments and things that might impact margin there and how we should model that business?

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Sure. So let's start with the first quarter gross margin, which was, as I said, very strong. We clearly did experience commodity inflation in the quarter. We experienced some year-over-year FX pressure as well. But we did have some nice pricing benefits. Jeff mentioned some of the things that we've done, in particular in Europe and some other markets around the world, that have been positive for us. He was referring more to last year, but we also some -- saw some of that impact this year in the first quarter. And then we also had focused on cost actions and productivity that came in very nicely throughout the quarter. And then we put a little bit of investment back into the P&L. So I think, probably the difference was -- is we didn't put quite as much investment back in the P&L as we originally were anticipating in the -- at the beginning of the quarter. But frankly, the rate was not dramatically better than we anticipated. It was just modestly better. As far as Craftsman goes, this year, as we said, it's about $0.08 of EPS impact for us. The margin impact will be relatively modest, not a big number. The -- there is a -- which many of you are aware of, there's an accounting aspect related to the royalty stream or the free royalty basically that we provided to Sears. That does have an annual impact each year. That will drive, frankly, a large part of the operating profit here in 2017. And then, as we move into 2018 and beyond, it would be more about the activities associated with driving organic growth, driving more profitability in the business through our supply chain and our manufacturing, et cetera, et cetera. And so I wouldn't expect a large number here in 2016 -- 2017, I'm sorry, based on what I just described. And also, just keep in mind, a large part of the operating margin will come from that accounting dynamic.

Operator

Robert Barry from Susquehanna is online with a question.

Robert Barry - *Susquehanna Financial Group, LLLP, Research Division - Senior Analyst*

I had a question on tools margins, I guess, in 2 parts. I mean, big picture, up over 100 basis points in 1Q. I mean, do you think you can maintain something close to that degree of kind of year-over-year progress? A lot of those drivers you mentioned seem like they could carry forward. And I think you were expecting even better performance in the back half due to lower launch costs. And then just kind of a sub question related to Newell synergies. What's the cadence of that $80 million to $90 million of cost synergies? I think that was by year 3. How much is coming in '17 versus in '18 and '19?

Donald Allan - *Stanley Black & Decker, Inc. - CFO and EVP*

Yes. So the gross margin, the trend -- I expect the trend to continue throughout the year. Can I guarantee every quarter will be perfect based on what we did in Q1? Absolutely not but -- because there is timing of when we make investments and various other factors. But the Tools & Storage business right now, although they have some headwinds, the headwinds aren't quite as large as what we've experienced over the last few years. Currency is a much lower number. Commodity inflation right now is a reasonable number. We'll continue to watch that as the year progresses, but in total, those numbers are about $100 million to $105 million, with a large part of that, probably 80% of that hitting the Tools & Storage business. So when I think of the business trend, and as I mentioned as I went through guidance, I think the trend is going to continue to be accretive year-over-year as we go throughout this year. And it won't necessarily be of the same magnitude every quarter based on what we had in Q1, but we definitely expect to have solid accretion. As far as Newell's cost synergies, we -- as Jeff mentioned, we've just started that process in the last 30 days. Good news is we had a fair amount of planning leading us to the closing, over about a 90- to 120-day period of time, so we were ready to go day 1, and -- which was -- which is always great to be in that position. And so this year, we think we're probably going to get about $20 million to $25 million of cost synergies from Newell in 2017, and the rest of it will kind of pace a little evenly over the next 3 years. So that would be what you should expect for 2017.

Operator

Liam Burke from Wunderlich is online with a question.

Liam D. Burke - *Wunderlich Securities Inc., Research Division - SVP*

On the industrial tools side of the business, Jim, you've mentioned strength. Was that across the board? Or were there any particular verticals that did well?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

We'll let Jeff tackle it since he's got industrial tools under him.

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

We were up strong mid -- or mid-single digits. It's about 7% in the Industrial business. That was pretty pervasive across all of our industrial tools businesses. The Tier 1 folks were up double digit in the quarter. So that recovery looks promising, and we believe our growth in that market certainly was a share gain more than just the market improvement, although the market did improve concurrent with our Q1 results. We did see some industrial tools folks actually exit the market, which we very quickly converted over to our brands, which was fantastic. So things like that as well as the FLEXVOLT introduction in those industrial channels has been really high -- really well done, well accepted and that technology really performing in that marketplace. So all those things come together for a market that has improved a little more than we expected, and our growth is greater than that market itself. So that's kind of the way we see it going forward.

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

So Jeff, while you're on the topic of FLEXVOLT, maybe you could just expand a little bit on the program right now. I know there's a little skepticism out there from a couple of people who probably have a vested interest in skepticism. So why don't you just tell -- give them the ground truth about FLEXVOLT right now?

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

What tends to be in this marketplace, competitors are violent. And if your competitors don't have a response, they tend to have a negative view on what you're doing and how it's performing. The reality is we couldn't be happier with FLEXVOLT. And if you think of 7% growth in this first quarter, 8% in North America, 6% in Europe, we're very pleased with that. But half that growth came from FLEXVOLT, half came from the core. So what it says is our core business is vibrant. We comped a very big quarter from last year and grew the core at the same time while allowing FLEXVOLT to provide the other half of the growth. Our retail execution of FLEXVOLT is now more than double digits ahead of what the customer expectations were, which is fantastic. And the uptick in -- or uptake in industrial channels, every bit as good, if not better. So if you consider those things and you look to the fact that we are loading new FLEXVOLT products as we speak in this quarter and we will continue to load new introductions throughout 2017 and, as Jim said, into the next several years, that has been the real driver behind what do you do with this breakthrough innovation team. We have to continue to keep this fresh, and we feel that we are quite nicely doing that. The last point I would tell you is, while it takes time to introduce new systems and power tools, the fact that this doesn't leave the old system behind has led to a much faster adoption than most new power tool platforms. As such, our growth in FLEXVOLT, the ramp in FLEXVOLT is 10x faster than the ramp in brushless, as an example. So we couldn't be more pleased, and we are -- we know it's a competitive advantage. And the average -- of 5 stars, the average user rating of FLEXVOLT is 4.9. So if you get the product right for the user, everything else takes care of itself. So we feel great.

Operator

David MacGregor from Longbow Research is online with a question.

David Sutherland MacGregor - *Longbow Research LLC - CEO, Director of Research and Senior Analyst*

Just while we're on FLEXVOLT, if we could maybe go back to Jeff and just talk about the development of 60- and 120-volt cordless tools. And how should we think about kind of the growth potential and the timing of those products?

Jeffery D. Ansell - *Stanley Black & Decker, Inc. - EVP of Global Tools & Storage and Group Executive*

Well, the beautiful thing about FLEXVOLT is we are able to develop 20-volt tools where they're appropriate, where the max watt out performance is appropriate; at the same time, develop 60-volt tools where the max watt out performance is required. And obviously, there's a cost difference, right? The 60-volt tool is a more expensive proposition for the user and for us, but it delivers unprecedented performance. At the same time, the user wants the right tool for the right job at the right cost. So all those things come together. And what you'll see over the next 36 months, we'll be presenting this to Jim and team in the next few weeks and then you'll see some of it at the May 16 session, you'll see fresh introductions of both 20-volt and 60-volt tools coming within the FLEXVOLT range. And I will tell you this. The users' pickup on them has been equivalent. The user likes what they can do with FLEXVOLT batteries on their 20-volt system, but they really have also embraced the 60-volt performance. Circular saw, in particular, is absolutely killing it. The portable -- you mentioned the 120 volt. The portable products like miter saws, which are 120 volt, absolutely killing it. So the user has embraced all those various platforms and -- because it gives them the performance of corded in a cordless package. So yes, more to follow, but yes, we're very, very active in development of 20-, 60- and even 120-volt tools going forward.

Operator

Robert Wertheimer from Barclays is online with a question.

Robert Cameron Wertheimer - *Barclays PLC, Research Division - Director and Senior Industrials Analyst*

Congratulations on getting all the deals done. Obviously, a lot of work and rapidly done. On Craftsman, is there -- I mean, what's your sense of scenarios and contingencies if Craftsman at Sears declines, for whatever reason, faster than expected? Do you have a current channel to absorb it? Do you think that the additional channels you might add are going to be in place in the near term?

James M. Loree - *Stanley Black & Decker, Inc. - CEO, President and Director*

I think we're planning for a more rapid ramp than $100 million a year over 10 years. We can probably handle a ramp, with our current planning, at about 2x rate of that. Clearly, that's hypothetical at this point in time and it's a contingency, but it's certainly -- definitely something that we're planning for in the event that, that were to occur.

Operator

We have no further questions at this time. I would now like to turn the call back to Greg Waybright for closing remarks.

Gregory Waybright - *Stanley Black & Decker, Inc. - VP of IR*

Chelsea, thank you. We'd like to thank everyone again for calling in this morning and for your participation on the call. But obviously, please contact me if you have any further questions. Thank you.

Operator

Ladies and gentlemen, this concludes today's conference. Thank you for participating. You may now disconnect.

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