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SWK - Q4 2017 Stanley Black & Decker Inc Earnings Call

EVENT DATE/TIME: JANUARY 24, 2018 / 1:00PM GMT

OVERVIEW:

Co. reported 2017 revenues of $12.7b and diluted EPS (excluding charges) of $7.45. 4Q17 revenues were $3.4b and diluted EPS was $2.18. Expects 2018 GAAP EPS (inclusive of various one-time charges related to M&A) to be $7.80-8.00.

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PRESENTATION

Operator

Welcome to the Fourth Quarter and Full Year 2017 Stanley Black & Decker Earnings Conference Call. My name is Shannon, 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, Dennis Lange. Mr. Lange, you may begin.

Dennis Lange - *Stanley Black & Decker, Inc. - VP of IR*

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

Our earnings release, which was issued earlier this morning, and a supplemental presentation, which we'll refer to during the call, are available on the IR section of our website. 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 our press release.

This morning, Jim, Don and Jeff will review our fourth quarter and full year 2017 results and various other matters followed by a Q&A session. And 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 is, therefore possible that actual results may materially differ from any forward-looking statements that we may 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.

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

Thanks, Dennis, and good morning, everyone. Thank you for joining us. As you saw in this morning's press release, we delivered a solid fourth quarter performance, bringing closure to an impressive 2017.

The company continued its above-market organic growth trajectory and delivered operating margin rate expansion, strong EPS growth and very good free cash flow conversion. This solid performance highlights the power of coupling our well-developed organic growth machine with a return to acquisitions. We're encouraged and we believe that this trend will continue into 2018.

Moving to the fourth quarter numbers. Revenues were $3.4 billion, up 17%, with organic growth of 8%. Acquisitions added 9 points of growth and currency contributed 3 points. These factors were partially offset by the Mechanical Security divestiture.

Tools & Storage continued its strong contribution, accelerating to 11% organic growth and 26% total growth with strength in all major geographies and business units. This performance reflects a vibrant series of growth initiatives around the globe and a stream of innovations that we have brought to the marketplace, including FLEXVOLT.

As expected, Industrial decelerated in the quarter to a still positive 2% organic, just ahead of our expectations. And all 3 Industrial businesses delivered growth in the fourth quarter, which was enough to more than offset anticipated declines in Engineered Fastening's electronics business as well as lower self-piercing rivet system sales.

Security ended the year with 2% organic growth, including modestly positive performances from both Europe and North America. And Don will provide you with a deeper dive into business-level operating performance during his remarks.

Our total company operating margin rate, excluding M&A-related charges, remained healthy and expanded 30 basis points versus prior year. EPS for the quarter was $2.18, a 27% expansion as strong operational execution was coupled with lower restructuring costs.

Also noteworthy, we reached agreement in late December to purchase the industrial-focused business of Nelson Fastener Systems for $440 million in cash. The agreement excludes Nelson's automotive stud welding business and is a right-down the fairway bolt-on for Engineered Fastening.

Nelson increases our presence in the general industrial end market, expands our portfolio of highly engineered fastening solutions and will deliver significant cost synergies relative to its size. Nelson's LTM revenues were approximately $200 million. The company employs about 700 people and operates 11 manufacturing sites. We expect the transaction to close in the first half of 2018 and look forward to integrating Nelson and adding scale and capabilities to Engineered Fastening.

Now let's turn to full year highlights. 2017 was a year of impressive financial performance, strong execution and progress toward our strategic objectives and our 22/22 Vision. Full year revenues were $12.7 billion, up 12%, including a 7% contribution from organic growth as well as a 7% contribution from acquisitions. Our operating margin rate expanded 40 basis points to a record 14.8%. Productivity and cost reduction initiatives supported a 40 basis point expansion in gross margin despite nearly $100 million of currency and commodity headwinds.

2017 was a case study of SFS 2.0 in action. Innovation, commercial excellence and digital excellence fueled above-market revenue growth and margin expansion. That growth, along with cost and asset efficiency from Functional Transformation and core SFS, enabled us to continue to make targeted investments to support future innovation, growth and margin expansion. All in all, a highly virtuous circle.

Ex charges, diluted EPS for the year was $7.45, a 14% increase and a new record for Stanley Black & Decker. Free cash flow remained robust at $976 million. And cash conversion came in at our target of approximately 100%.

Turning to portfolio strategy. 2017 was a year in which we executed several significant portfolio moves. The year began with a $725 million tax-efficient Mechanical Security divestiture, which was followed by the acquisitions of the Craftsman brand and Newell Tools, which combined, totaled approximately $2.9 billion. In doing so, we added 3 iconic brands, Lenox, Irwin and Craftsman, with a far greater future growth potential.

Specific to Newell Tools, we continue to execute plans to integrate employees, suppliers and customers into our operations. We remain focused on and confident in our ability to capture the $80 million to $90 million of cost synergies. Our commercial teams continue to refine plans to pursue revenue synergies as well. In that regard, we will move to global execution mode this year and begin to drive meaningful results in that area.

And turning to Craftsman. We continue to make great progress on product development, supply chain deployment and commercial strategy. The Tools & Storage folks, along with our customers, are in full-bore execution mode of internally and with our partners and are confident that the mid-2018 rollout will be a successful relaunch of this incredibly strong brand. And additionally, we've made further substantive progress on the commercial strategy. And Jeff Ansell will provide some more color on that in just a few moments. So as you can see, we remain on or ahead of our plans as it relates to the integrations.

In summary, 2017 was a really great year for Stanley Black & Decker. What a special performance by our 57,000 employees around the globe. I thank them for their dedication, agility and will to win because it is our people to whom we attribute these great accomplishments. They live our purpose every day with incredible passion.

2018 looks to be shaping up to be another strong year as we celebrate our 175th year in business on a high note. We have generally supportive market conditions with a few minor exceptions within Industrial, a strong pipeline of acquisitions and organic growth initiatives developed in accordance with SFS 2.0. We have a cost and productivity focus that supports margin expansion and is the bedrock of our operating system as well as a host of new opportunities related to our innovation activities.

And as always, we have to navigate known headwinds, such as commodity inflation and other unknown pressures, that may arise. We feel that we positioned the company for a successful 2018, nonetheless.

And now I'll hand it over to Don Allan, who will walk you through segment performance, overall financials and 2018 guidance. Don?

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Thank you, Jim, and good morning, everyone. I will now take a deeper dive into our business segment results for the fourth quarter.

Starting with Tools & Storage. Revenues were up 26% in the quarter with an impressive 11% organic growth, 13 points of acquisitive growth and 2 points of currency. The operating margin rate for this segment was robust at 16.7% as benefits of volume leverage and productivity more than offset growth investments, commodity inflation and price to support normal holiday promotions, yielding a 50 basis point expansion versus prior year.

The strong organic growth and related share gains were experienced across each Tools & Storage region and SBU. On a geographic basis, North America was up 8% organically with strong performances across all channels. The U.S. commercial market generated double-digit growth, U.S. retail channel posted high single-digit growth and our industrial and auto repair markets generated mid-single-digit growth. Additionally, Canada contributed solid organic growth of 8%.

North America's growth continued to be fueled by strong commercial execution and product introductions across the portfolio, including contributions from FLEXVOLT. We continue to see very little cannibalization impacts from the FLEXVOLT launch and are seeing more positive indications that this is stimulating incremental demand for our DEWALT 20-volt cordless power tool system while also not impeding growth in corded products. Our shipments continued to be supported by strong demand in the channel as North America POS was up mid-single digits and inventories within our major customers were also in line with prior year levels.

Europe delivered another outstanding performance with 17% organic growth. 10 out of 10 markets grew organically with double-digit performances in 8 of the markets, including the U.K., France, Iberia and Central Europe. The team continues to leverage our portfolio of brands and expand on our retail relationships to produce sustained above-market organic growth. This performance exceeded our recent trend of mid- to high single-digit performances as the region benefited from a strong holiday season.

Finally, emerging markets delivered another quarter of outstanding organic growth, up 17%, with all regions delivering double-digit performances. Diligent pricing actions, continued e-commerce strength and the ongoing MPP launch across the developing markets continue to support growth. Geographically, Latin America was very strong, headlined by double-digit growth in Brazil, Argentina and Mexico while Peru and Chile delivered high single-digit results. Our change to a direct selling model within Turkey and Russia continued to fuel exceptional growth for those countries. In addition, Korea, Japan, India and China posted notable double-digit growth.

Within the Tools & Storage SBUs, all lines showed high single- to double-digit growth in the quarter. The power tool and equipment group was up 13% organically, led by professional power tools at 15%. This SBU also benefited from new product introductions, reflecting core innovation as well as FLEXVOLT, along with continued strong commercial execution. Our hand tools, accessories and storage organization generated 9% growth on new product introductions and strong performances within the construction and industrial end markets.

The accessories segment was up 14% while hand tools and storage delivered 8% growth, another nice performance from this team while they are also successfully continuing to integrate Lenox, Irwin and the Craftsman brand. So in summary, truly an outstanding quarter and an outstanding year for the Tools & Storage organization. Jeff will provide some additional color on the full year in a few minutes.

Turning to Industrial. This segment delivered 2% organic growth, as Jim mentioned, slightly ahead of internal expectations. This top line performance contributed to an 80 basis point expansion in operating margin rate from volume leverage, productivity and cost control. Engineered Fastening posted 1% organic growth during the quarter, with mid-single-digit growth in automotive and industrial, which more than offset lower electronics volumes.

Within automotive, growth was led by continued penetration gains within fasteners, enabling organic growth well in excess of light vehicle production. This more than offset the expected impact of lower self-piercing rivet systems sales due to lower model rollover activity on our automotive customers. Finally, the growth within the general industrial fastener market reflected supportive market conditions and enhanced commercial actions, enabling share gain within our customer base.

The Infrastructure businesses posted a strong quarter, up 8% organically. Hydraulic Tools grew 19% as it continues to see the benefits from the execution of successful commercial actions as well as a supportive market environment. This team continues to raise the bar for commercial excellence as all regions contributed to growth.

Meanwhile, Oil & Gas generated 3% organic growth in the quarter, driven by North America auto weld and inspection project activities, which more than offset a continued and expected decline in offshore project activity. The North America inspection business has been a relatively new driver for organic growth and outperformance for Oil & Gas. The team's commercial efforts have grown this business from approximately $15 million in 2016 to nearly $50 million this year.

Finally, the Security segment delivered 2% organic growth during the quarter. North America organic growth was up 2% due to higher installation activity within convergent security systems and higher product volumes within health care. Europe organic growth was up 1% as strength in the Nordics and the U.K. were offset by anticipated ongoing weakness in France.

In terms of profitability, the segment declined 200 basis points year-over-year. The sale of the mechanical locks business drove approximately 90 basis points of this contraction. The remaining 110 basis point decline was attributable to mix and modest levels of investment to support long-term growth. The mix impacts came about due to higher mix of installation revenues within CSS, lower software sales within health care, and then country mix within Europe.

It is important to note this operating margin was consistent with the performance of the business over the last 2 quarters. Security team remains focused on innovation, along with commercial and operational effectiveness, to position the business for revenue growth and margin expansion in 2018.

Let's take a look at the free cash flow performance on the next page. In addition to the strong P&L performance, we were able to drive significant working capital improvements during the quarter. Our full year cash flow performance was strong as we generated $976 million in 2017. Versus 2016, cash from operations declined $66 million. However, this included a $261 million investment in working capital, which was $318 million higher than 2016 to support the very strong levels of organic growth, most notably within Tools & Storage. This impact was partially offset by higher cash earnings from the business.

In addition, we saw our capital expenditures increase by $96 million in 2017 as we made investments to expand our manufacturing and distribution capacity as well as investments to support acquisition integrations. This performance resulted in free cash flow as a percentage of net income to be approximately 100% when excluding the net gain on divestitures, right in line with our stated financial objective.

From a working capital turn perspective, we delivered 8.9 turns in the fourth quarter, a decrease of 1.7 turns versus the prior year. This decline reflects the impact of our recent portfolio activities, specifically the acquisitions of the Lenox, Irwin and Craftsman brands. Excluding these acquisitions, turns were 10.6x, consistent with our record 2016 performance.

Working capital management remains a key pillar of the SFS 2.0 operating system. We continue to drive working capital improvements across the company. With heavy focus on improving the performance of our recent acquisitions such as Newell Tools, we are confident in our ability to now bring our working capital turns back above 10 in the coming years.

I would now like to take a minute to provide some comments regarding the recently enacted U.S. tax legislation and its respective impact to the fourth quarter 2017 and full year of 2018. We expect these changes to deliver a positive impact to the U.S. economy and are very supportive of the improved worldwide cash mobility that comes with the territorial tax system and finally encouraged by the benefits that come from the lower effective tax rate.

In the fourth quarter, we recorded a onetime $24 million net tax charge, which is reflected in our GAAP EPS. This includes an estimated liability of $466 million to reflect the new territorial toll charge. As you know, this is payable over the course of 8 years, heavily weighted to 2022 and beyond. Partially offsetting this is the positive impact from remeasuring our net deferred tax liability positions at these new lower tax rates. Keep in mind, the regulatory guidance surrounding this new tax bill continues to be refined and the fourth quarter charge is based on current estimates. We will finalize the overall impact during 2018 as we receive refined guidance from the U.S. Treasury Department.

Now turning to the impact to the 2018 effective tax rate. The full benefit of the decrease in the U.S. tax rate from 35% to 21% is estimated to be approximately 5 points on our effective tax rate. This benefit, however, is mitigated by approximately 3 points of tax costs from certain new provisions in the tax law as well as reduced benefits from previously allowed deductions. Our guidance for 2018 will be based on a tax rate of approximately 18%, which is a $0.20 EPS benefit versus 2017. Hence, the overall estimated impact of the new legislation is a 2 point benefit to our effective tax rate in 2018.

Now let's move deeper into our 2018 guidance. Before I start, this outlook is based on the first quarter adoption of 2 new accounting standards with respect to revenue recognition and pension accounting. For financial modeling purposes, we released a supplementary 8-K this morning to provide the impacts to operating results and business segment information for 2016 and 2017. The impact from these changes has a modest negative impact on our operating margin rates and is relatively neutral to EPS.

We are targeting approximately 5% organic growth in 2018, which will result in adjusted earnings per share range of $8.30 up to $8.50, which is an increase of approximately 13% versus the prior year at the midpoint. And we expect our free cash flow conversion to approximate 100% again in 2018. On a GAAP basis, we expect the earnings per share range to be $7.80 up to $8, inclusive of various onetime charges related to M&A.

You can see on the left side of this chart, we expect the benefits from organic growth to generate $0.50 to $0.60 of EPS accretion. This will be partially offset from $0.25 to $0.30 of net commodity inflation, which includes approximately $150 million of commodity pressure, which will be offset by the impact from pricing actions that will begin to be reflected in the P&L as we move into the later stages of the second quarter. Across the full year, this reflects a 60% to 70% price recovery.

Next, we expect the net impact of cost and productivity actions, acquisition accretion and a higher share count year-over-year to deliver a positive $0.45 to $0.50 in EPS. As previously mentioned, we expect the tax rate of approximately at 18%, which will deliver, as I mentioned, $0.20 in EPS accretion.

A few other housekeeping items I'd like to review that we referred to as other miscellaneous guided matters. The first is that we continue to anticipate approximately $50 million of core restructuring charges, which is consistent with the last few years. Second, we are forecasting approximately 155 million shares outstanding for 2018.

Finally, we expect the first quarter's earnings to be approximately 16% of the full year performance. This is about 130 basis points lower than last year. The primary factor driving the lower percentage of full year delivery is that we continue to expect elevated levels of commodity inflation, particularly in tools, but do not expect to see the price recovery benefit until we get into the later stages of the second quarter and beyond. The net price/cost headwind for the first quarter is expected to be approximately $50 million. This impact is somewhat mitigated by lower below-the-line expenses year-over-year due to the onetime environmental and pension charges that were taken in the first quarter of last year.

Now let's turn to the segment outlook on the right side of the page. Organic growth within Tools & Storage is expected to be mid-single digits in 2018. There are multiple organic growth catalysts, including core innovation, continued benefits from FLEXVOLT, the start of Lenox and Irwin revenue synergies, emerging market growth and perhaps most exciting, the Craftsman brand rollout in the second half of the year. Another positive factor is that we are generally seeing supportive markets across most geographies that we serve. We believe the top line growth will translate into an improved margin rate year-over-year.

As many of you know, the rollout of the Craftsman brand will have somewhat of a governing factor on how far we can push margins forward in tools next year as it will begin at below-line average profitability. This dynamic is due to heavily relying on our outsourced providers as we ramp up in the marketplace. And over time, we will improve profitability as we in-source production.

In the Industrial segment, we expect low single-digit decline in organic growth. Within Engineered Fastening, we expect to see relatively flat organic performance. We will see above-market growth within automotive and industrial fasteners. But that will be offset by lower automotive system sales due to a decline in model rollovers at our automotive customers and the residual comp issues within electronics, most notably in 1Q.

In Oil & Gas, we expect to see a double-digit decline due to lower onshore project activity across the pipeline market. And then within Hydraulic Tools, we expect to see continued growth from our successful commercial actions. With the team's proactive costs and productivity focus, we expect Industrial operating margins to improve in this segment for the year.

Finally, in the Security segment, we are expecting the organic growth to be up low single digits in 2018 as the team continues the commercial momentum from 2017. This should translate into improved operating margins year-over-year as we drive our cost and service productivity focus.

So in summary, we believe that we are taking the appropriate actions to position the company for earnings growth and margin expansion in 2018, which is consistent with our long-term financial targets. We remain focused on free cash flow generation, acquisition integrations and the rollout of the Craftsman brand. So as you can see, there's a lot to be excited about in 2018.

With that, I would like to turn the call over to Jeff for a few key full year Tools & Storage highlights, and then a brief update regarding Craftsman. Jeff?

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

Thank you, Don. 2017 was a special year for our Tools & Storage business, including expansion of operating margins while delivering 9% organic growth and 19% total growth. This translates to $1.4 billion in growth with approximately half coming from organic initiatives and half from acquisitions, an accomplishment that used to take years rather than months to achieve. We delivered market-leading innovation, quality and commercial excellence. And as such, we were recognized with vendor awards from the largest customers across every channel and every geography.

We expanded our exclusive FLEXVOLT system, which offers the user the power of corded with the freedom of cordless. This innovation spearheaded and accelerated DEWALT growth across corded products, 20-volt cordless products and across the FLEXVOLT range itself. DEWALT was the only provider with growth across corded products as well as low- and high-voltage cordless products concurrently.

Our stable of brands continued to perform well on a global basis with Stanley, Black & Decker, Mac Tools all up single digits while Proto, Vidmar and DEWALT all expanded double digits. All of this occurred in consort with the successful integration of our second- and fourth-largest acquisitions in our history, namely Irwin, Lenox and Craftsman.

To close the book on 2017, we delivered growth across every region, every channel, every strategic business unit and with all of our top customers. We integrated a complex carve-out in Newell Tools and built Craftsman from the ground-up, all concurrent with delivery of our largest organic growth year in history.

Looking to 2018, and as Jim mentioned earlier, I am also pleased to provide an update on our plans for the Craftsman brand going forward. During the October earnings call, we provided an update on the development of our Craftsman distribution strategy. That update included confirmation that Ace would support Craftsman across the hardware channel and Lowe's would support Craftsman across the home center channel.

As we continue to develop and fine-tune this strategy, we are pleased to confirm that we will also make Craftsman available via Amazon. With support from leading companies like Lowe's, Ace and Amazon, we expect to make Craftsman available to far more users than any time in its 90-year history. Overall, the support of the iconic Craftsman brand to date is overwhelming.

Now I'll turn the call back to Jim to wrap up today's presentation.

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

Thanks, Jeff, and a great year, lots of exciting news. And for the total company, in summary, 2017 was another strong year of execution and financial performance. And just to reflect one last time: 7% organic growth, 7% contribution from acquisitions, a 40 basis point expansion in operating margin rate, a record 14.8% and 14% EPS expansion.

We reshaped the portfolio with the divestiture of Mechanical Security, purchase of Newell Tools and the Craftsman brand. And these transactions, as Jeff said, are on track and some of the exciting benefits from them are just on the horizon. And '18 is shaping up to be another strong year with 5% organic growth, 11% to 14% EPS growth. And we're encouraged by the many, many organic growth catalysts across the company, catalyzed by SFS 2.0 and a great execution team and also arising through our recent acquisitions.

And I'd like to thank my senior management team, our 57,000 associates and all our stakeholders, including the investment community, for your strong support as I reflect back on 2017, my first full year as CEO. Our deep and agile leadership team, along with our entire employee base, remain focused, committed and supportive as we tackle 2018 to deliver strong above-market organic growth with operating leverage and continue to successfully integrate these acquisitions and generate strong free cash flow.

And additionally, we're energized, our team is energized by our company's purpose: for those who make the world to achieve our 22/22 Vision and to strive to become known as one of the world's leading innovators to deliver top-quartile financial performance and to elevate our commitment to corporate social responsibility.

And Dennis, we're now ready for Q&A.

Dennis Lange - *Stanley Black & Decker, Inc. - VP of IR*

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Rich Kwas with Wells Fargo Securities.

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

Jim, on Craftsman, first of all, can you give -- shed any light on timing, how we should think about this as the rollout in terms of timing? And then second, Don, I didn't see anything with regards to the FX assumptions within the guidance. And then what's your comfort level with commodity costs at $150 million? That's unchanged from what you talked about in November. And metals prices have gone up here recently. So just some additional thoughts there.

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

Sure. On Craftsman, I'm going -- well, you snuck in two questions, by the way. We obviously said one. How did that happen? Anyhow, on Craftsman, there's a lot of variables on Craftsman. It's interesting, when you think about Craftsman, we bought a brand and maybe like 3 people along with it. And the work that the team has been doing and consumed by for the last year or so is an incredible execution project, multidimensional, et cetera. The relationships, as Jeff pointed out, are going extremely well on the commercial side. The supply chain work is going extremely well. And frankly, we're super excited about it as I'm sure you can appreciate. As for timing, I'm going to ask Jeff to comment on that because he's managing all these -- juggling all these balls at the same time here. And I'll turn it over to you for a moment there, Jeff, on that one.

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

Thanks, Jim. To answer the question, we've built a dedicated Craftsman team and built them up so that the core business continues to accelerate even while we build Craftsman from the ground-up. We're in development of the new products to go with the brand that we acquired. And until that is complete, we really can't effectively do capacity planning, which is just beginning as we speak. While we're committed to launching Craftsman in the second half of the year, customer rollout plans will be dependent on the completion of the customer demand plans, along with our capacity plan to ensure supply. As stated earlier, the support of this iconic brand is overwhelming. And our teams engage to support as much demand as possible -- as soon as possible. However, it is clear at this point that we will have greater demand than supply in 2018.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

So I'll take the second question that Rich snuck in there. On the commodity side of $150 million at this stage, that would be representative of current prices. What our view is that would impact our P&L. We're -- like always, we do contingency planning, and we're focused on if another $30 million or $50 million of commodity inflation came our way, how would we react. So that is factored into our thought process and in our contingency planning. The FX question, for a long time, it was a modest negative. It flipped to a modest positive, in particular because of what's happened with the euro and the pound as it strengthened against the U.S. dollar. But we have seen a little bit of an offset in emerging markets, where the dollar has been strengthening against some of the key emerging market currencies. But right now, it's day-to-day or week-to-week, it's kind of swinging between a net positive and a net negative. So relatively minor impact to us at this stage and really not something we're calling out as a major assumption in our guidance. But clearly it is something we continue to focus on for contingency planning.

Operator

Our next question comes from Michael Rehaut with JPMorgan.

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

I also just wanted to hit on a couple of short questions, if possible. First, in terms of the guidance, focusing on the shares outstanding and the amount of free cash flow conversion, obviously you announced the acquisition, which would take a portion of that. But I was wondering around your thoughts on share repurchase. That's something that you do on and off. And with the strong free cash flow in 2018, absent any additional acquisitions, is that something that we should be thinking about as you get into the year? And then just secondly on Craftsman, when should we expect sort of a shift towards in-sourcing some of the production that could cause a lift to the margins in that sales bucket?

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

Sure. It's Jim. I'll take the first question, and I'll ask Don to tackle the second one. And he may get a little help and color from Jeff as well, okay? So on repurchase, let's just jump to the kind of a little more in altitude to capital allocation in general. And over the courses of as long as Don Allan, Jeff Ansell and I have been a part of this company, we've had a capital allocation strategy of giving 50% of our excess capital back to shareholders, and then taking the other 50% and reinvesting. And when you look at the dividend today is running a little over $300 million, we're throwing off $1 billion, but that's a growing number now. So there's definitely -- when you look at that long-term framework, there's definitely room for repurchases. And we historically have repurchased. And we've done it at times when we thought the stock was severely undervalued in general. And occasionally, we've also, from time to time, used it to manage the share count to kind of neutral as employee benefit types of dilution occurred or also when we had significant stock price increases and that might create some additional share count. So we've done all of that. But I think right now, with the acquisitions that we've made, and recently now another $440 million, and a pipeline that is really, really strong in the acquisition area, in fact, we're executing integrations as effectively and quickly as we can in order to begin to create some organizational bandwidth for bringing some more acquisitions on. So with all that going on, repurchase is fairly well on our list of capital allocation priorities. But that could change. We think about it over the long term, and then we operate tactically in the short term based on a myriad of different observations and considerations. And so with that, I'll turn it over to my colleagues here for the second question.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Okay. I'll just start and just remind people of what we've said in the past about Craftsman and pulling that into our supply chain and our manufacturing plans. And I'll let Jeff give a little more color on what we're thinking over the next few years. But in essence, what we've said is that really it would be kind of a 3-year program of in-sourcing a large amount of these Craftsman products into our, not all of them but a large amount of them, into our manufacturing and supply chain. And it would be something of a bit of a gradual impact over that 3-year time horizon. Jeff commented this morning that we still have a lot of work to do around capacity planning. And we're in the process of doing that. So we don't have all the answers to it, but we do believe it will be a multiyear transition period. But Jeff, why don't you provide a little more color on that?

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

So if you consider what we have to do in the core business side-by-side with what we are doing concurrently in the Craftsman business, we'll launch about 1,000 new products in our core business every year and we'll make about 85% of all those products that we sell around the world. So we're the most innovative tool company in the world and also we make the highest percentage of what we sell. That won't change and it can't change because our core business continues to -- has to continue to perform well. Concurrent with that, we have to bring up several thousand Craftsman products. So imagine this, we'll launch 1,000 product in our core, we have to launch 2,000 Craftsman products around at the same time. Now we're capable of doing that. At the same time, we want to repatriate Craftsman manufacturing as much as possible to the United States. So we made an acquisition in 2017 of the preeminent metal tool manufacturer in Waterloo that is a dedicated Craftsman manufacturing facility, which is one of the things we committed to. So we will bring up that manufacturing of Craftsman products, we will make more than half those products in year 1. And we'll make probably more than half of those products in the United States in year 1. But as Don said, it will take probably a 36-month period before we get to the point where we are making the same percentage of the Craftsman product as we make in our core. But I think over a 3-year period, we can certainly get there and we can repatriate much of that to the U.S. to stand behind the Craftsman brand promise.

Operator

Our next question comes from Steven Winoker with UBS.

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

This is Chris for Steve. So just kind of back to the Craftsman topic, originally you guys have said that it was going to generate like $100 million of incremental sales every year. I'm just kind of curious, like with a lot that's going on, on the Sears brand closing stores, how do you guys think about that number now in terms of the expectations going forward?

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Well, we still feel like the opportunity is very significant. It's very difficult to gauge at this stage any change that we should make to that assumption. That assumption was based on what we believe were very reasonable factors. And I think as we get deeper into this planning process that Jeff just described a few minutes ago, things will come to light and we'll indicate how quickly this ramp will go. But we're at the very early stage of this process. And so at this point, we're not looking to change anything around those assumptions. But as we get deeper into the Lowe's rollout, when Amazon goes online at some point, which at this stage, we'll probably provide an updated view on what we think the Craftsman brand will do. But it's far too early here sitting in January to really alter those assumptions.

Operator

Our next question comes from Tim Wojs with Baird.

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

I guess just turning maybe to the margins a little bit. I was wondering if you can maybe give us a little bit of color on just the cadence within the tools business. Just given the price/cost headwinds may be in the first quarter and then how Craftsman kind of ramps, how should we think about tools margins as you go through the year?

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Sure. So the first quarter clearly will be pressured because of kind of that $50 million of kind of net price commodity cost headwind I mentioned. So for the tools business, you will see a rate decline year-over-year in the first quarter because of that. And we also had an outstanding first quarter last year from a rate perspective for tools. And so you have a difficult comp, and then you have this dynamic I just described. So it will be down a little bit year-over-year because of that. But as the year progresses, you'll see that get better and better. It will probably be modestly down in the second quarter, and then it will start to show improvement year-over-year in the third and the fourth quarter. And it's really because of that dynamic of commodity inflation hitting us pretty hard in the first half without the price recovery not coming until later stages of the second quarter and the back half of the year.

Operator

Our next question comes from Scott Rednor with Zelman & Associates.

Scott L. Rednor - *Zelman & Associates LLC - Director*

My question was on the mid-teens POS noted at the -- at your large retailers in Tools & Storage. So for whoever wants to answer that, it seems like that's been a little slower than the prior quarters. So just curious if you guys could provide some context there, whether there was a significant comp last year or kind of how you guys are thinking about that relative to the optimistic commentary.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Yes, what I said was mid-single-digit POS, not mid-teens, although we would really love mid-teens, but it was mid-single digits. And when I look at POS, you can't really go crazy analyzing it quarter-by-quarter. You have to look at it over a multi-quarter period of time. And if you look at the North American business, because I was commenting about POS in North America for certain customers, it was a little bit lower than the performance in North America, a couple of points. However, when you look at it over the entire year, it's very much in line with the performance of our revenue performance for North America versus POS for the year. So that's the best way to look it. The other thing to remember is that we had really strong performance outside of some of our retailers in North America in the fourth quarter, low double-digit performance in the commercial channel. So you have to keep that in mind as well. That's really pushing that number up in a positive way. So truly, those 2 factors. And again, like we've mentioned before, quarter-to-quarter POS is an important statistic to look at, but it's more about the trend that you're seeing and what you're experiencing over multi-quarters.

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

And Jeff is going to add something, I think.

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

Thank you. In addition, I would say we look at this, as Don said, over a 4-quarter kind of time, a rolling 4-quarter basis. And when looked at that way, you can see clearly that we've outgrown the market 2x. And the other feedback that we've received is from the customers, the largest of our top 10 customers, we've received vendor of the year awards because our POS would outpaced their overall growth in the category. So what that would tell me is that the POS is greater than the market, it's greater than our largest customers and weeks of supply are in line with the prior year. So that says that the things that we're putting in are going through the other end of the process in POS. And we feel very good about global POS in total as much as we can gather.

Operator

Our next question comes from Josh Pokrzywinski with Wolfe Research.

Joshua Charles Pokrzywinski - *Wolfe Research, LLC - Director & Diversified Industrials Analyst*

Just to follow up on the Craftsman commentary, and Don, not really deviating off that $100 million of incremental revenue a year. I guess if I look at your organic growth guidance and the EPS associated with that, it seems like incremental margins, knowing that raw materials are a different line item, are a little light versus where you'd be historically. If I assume that $100 million comes in at virtually no profitability, it still seems like it's at league average or not. Is there an indication that as Craftsman ramps up this year that the launch costs chip away at that profitability in a more material way? Or I guess, just kind of help us bridge how that base incremental margin looks a little lighter than usual.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Yes, I think the best way to think about it is that the leverage that we put in our guidance has a couple of factors in it. Clearly, one is what you're describing. There's a little bit of kind of launch cost and cost associated with Craftsman that has to be factored in, into that at lower profitability. And they certainly will be a nice component of our organic growth in 2018. The other thing to consider is that we've been on a steady program of investing for future growth in general as a company. And so as we get growth organically, we look at what investments we want to make in certain areas to continue to drive this growth over the mid-term and the long term. And so therefore, the leverage numbers you see are a little bit lower because of that as well. So it's really those 2 factors that are driving that dynamic that you're now describing.

Operator

Our next question comes from Mike Wood with Nomura Instinet.

Mason Marion

This is Mason on for Mike. Could you give us an update on FLEXVOLT sales? How many FLEXVOLT SKUs now have been rolled out? And what are the initial number of FLEXVOLT product expected in 2018?

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

So as I indicated in my presentation, we -- and I'll kick this over to Jeff for additional commentary. We were in line with our expectations for FLEXVOLT. FLEXVOLT will be a contributor to our guidance next year and our organic growth of 5% as a company. And it continues to be a very positive performer for us. But I'll ask Jeff to give a little more color on that.

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

Yes, we could be happier with FLEXVOLT performance. If you look at the adoption rate, it's still running at about 10x in terms of speed of adoption versus key technologies like brushless, which are fantastic. So that's a great endorsement of what it does for the user. At this point, we average about 4.9 stars on ratings around the world. And that's 18 months or 15 months into the process. That's the highest ratings we've ever achieved, so tremendous reviews. And what we've seen occur is, as I kind of intimated in my remarks, we've seen our corded product that we make where we sell, which is a differentiator for us, we've seen that up mid-single digits while the category was down about mid-single digits. Our 20-volt range has grown faster than any time in history. At the same time, FLEXVOLT itself has grown dramatically. So if you add those 3 things together, it says that there isn't cannibalization to us. There may be in the market, but it's someone else's cannibalization. We launched key new products in the fourth quarter and the second half of last year, things like cordless FLEXVOLT compressor that is revolutionary, is doing incredibly well. A new FLEXVOLT worm drive style saw that is absolutely converting corded products for the first time in history to cordless with more to follow in 2018. The point I would make there, though, as we continue to launch FLEXVOLT, we'll launch more and more Industrial products as we can get more and more output and capacity from these products. But if you consider the fact that in the last year, we've put enough FLEXVOLT batteries into the market to drive out cross-country 150x if it were an electric car, we are incredibly proud of what FLEXVOLT has done for us.

Operator

Our next question comes from Rob Wertheimer with Melius Research.

Robert Cameron Wertheimer - *Melius Research LLC - Founding Partner, Director of Research & Research Analyst of Global Machinery*

The question is on 4Q margin in Tools & Storage. And obviously, you guys have got a lot going on and have achieved a lot. Sequentially, maybe it was a bit lighter than we might have thought. And you've got commodity. I mean, I wanted to ask if commodity was the driver of that, if there's any excess freight, any production tangles or just inefficiencies from the extreme growth that you're seeing or whether it's just the investment. Just that's the question.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Yes, Rob, it's actually -- we were very pleased with the margin performance of tools, and as I mentioned, 50 basis point improvement year-over-year, incredibly strong organic growth. However, yes, I mean, there's a little bit of pressure on the margins for some of those things you mentioned. Commodity inflation continues to be something that we experienced in the fourth quarter that rolls into this year with really no price recovery in the fourth quarter. And then I would say there was modest freight increases associated with the high level of organic growth but nothing that really dramatically moved the needle in the business. But I think the major factor was more related to commodity inflation.

Operator

Our next question comes from Ken Zener with KeyBanc Capital Markets.

Kenneth Robinson Zener - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Jeff, and Don, and everybody, Jim, the cannibalism, I think that's the most incremental piece of information you communicated today beyond your execution. Why do I say that? Well, FLEXVOLT, if you're growing DEWALT, that almost means you are extending your brand awareness in your product as people (inaudible) your portfolio of tools, not someone else's. Why do you think -- and Jeff, you gave us those numbers. But why do you think that's happening? Why didn't you anticipate it? And most importantly, what are the implications as you continue to kind of drive core battery into what had been corded and/or what will be gas eventually?

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

So you asked Jeff, and then you asked Don, and then you asked me. So I'm going to have to -- and maybe I'll chime in. But the FLEXVOLT initiative and program has been, I think, a tremendous brand development and brand halo and had an effect on what was already an amazingly strong brand in the professional guaranteed tough kind of segment. And FLEXVOLT just takes it to another level. So that's one thing. I think the second thing is, and I've said this before, the installed base that we're developing of batteries that work on 60-volt FLEXVOLT tools and 20-volt tools, the FLEXVOLT battery obviously works on -- is backwards-compatible for the 20-volt. So when you start to develop this installed base of batteries and all of a sudden, you have the user has the functionality to be able to run the tool effectively 3 times longer on a 20-volt tool, that is a real kind of value driver and value proposition advantage for FLEXVOLT. So I think that was sort of one of the things that we wondered how effective that impact would be. And I think what we're finding out is it's probably very, very significant. And so that's my two cents on it. Then I'll turn it over to Jeff and see if you have anything more you want to add to that.

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

Well, if you go back in time to when Stanley Black & Decker came together, you would look at DEWALT, which was a fantastic brand franchise that probably was at a period of decline, given the technology change, where it offered NiCad and the world had moved to lithium. Fast-forward to where we are today and a couple of stats for you, we now make DEWALT in the United States, which competitors cannot do in power tools. We've expanded that DEWALT brand promise to tremendous hand tools, to storage products, lasers, all great products. We introduced our lithium ion answer in 2011 and '12. And a stat that you wouldn't be aware of, we're now 3x bigger in lithium than we ever were at our peak in NiCad. So that is an awesome statement. We've introduced brushless at the same time. Brushless is now bigger than NiCad ever was. And on top of that, we've improved our reliability, the highest reliably in the industry, greatest number of innovations. And add FLEXVOLT on top of that, and you're seeing what can happen. The user who always loved DEWALT now has so many more reasons to love, embrace and endorse it. And we're seeing the level of commitment to DEWALT has never been higher. And we're pleased with that.

Operator

Our next question comes from David McGregor with Longbow Research.

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

If I could just pick up for clarification on Ken's question, then I want to ask some other question on FLEXVOLT. But regarding the cannibalization, are we at a point where you could assume that the FLEXVOLT growth going forward is largely incremental? Or is there a reason to believe that cannibalization could be a future threat and emerge at some future point? And I guess, my question more on the margins was that FLEXVOLT running below tool segment average. Is that due to launch costs and heavy promotional expense, et cetera, and once we get beyond the launch, percentage margins on FLEXVOLT are expected to exceed the segment average? Or is this line expected to be at or below segment average margins for the foreseeable future?

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

I'll give the margin question to Don. But the way I'm thinking about FLEXVOLT at this point, it's going to be a steady contributor to our organic growth as time goes on, and it's -- at this point, it's hard to really understand FLEXVOLT versus 20-volt versus corded and whether all the dynamics, other than we know, what's already been said, which is it's a positive mix of effects. And in that regard, I think it's going to continue to be a real catalyst for above-market organic growth for Stanley Black & Decker and for DEWALT.

Donald Allan - *Stanley Black & Decker, Inc. - Executive VP & CFO*

Yes, on the margin question on FLEXVOLT, yes, I would say that we did have that period of time where we were below line average. It probably extended a little longer than originally projected because of some of the investments we were making around marketing, in particular to really make sure that people understood the technology, and how impactful it is. And clearly, some of the comments you're hearing from Jim and Jeff would indicate that, that is the case. So as we go into 2018, we would expect it to be right around line average margins. And it's not something that would be a negative to the margin or a dramatic positive at this stage.

Operator

Thank you. This concludes the Q&A session. I would now like to turn the call back over to Dennis Lange for closing remarks.

Dennis Lange - *Stanley Black & Decker, Inc. - VP of IR*

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

Operator

Ladies and gentlemen, this concludes today's conference. Thanks for your participation, and have a wonderful day.

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