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SWK - Q3 2015 Stanley Black & Decker Inc Earnings Call

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OVERVIEW:

Co. reported 3Q15 fully diluted EPS of $1.55. Expects 2015 full-year GAAP EPS to be $5.80-5.95.

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PRESENTATION

Operator

Welcome to the third-quarter 2015 Stanley Black & Decker earnings conference call.

(Operator Instructions)

Please note that this conference is being recorded. I will now turn the call over to the Vice President of Investor and Government Relations, Greg Waybright. Mr. Waybright, you may begin.

Greg Waybright - *Stanley Black & Decker, Inc. - VP, Investor & Government Relations*

Thank you, Stephanie. Good morning everyone and thanks for joining us for Stanley Black & Decker's third-quarter 2015 conference call. On the call in addition to myself is John Lundgren, Chairman and CEO; Jim Loree, President and COO; and Don Allan, Senior Vice President and CFO.

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 applications. A replay of this morning's call will also be available beginning at 2 p.m. today. The replay number and the access code are in our press release.

This morning John, Jim and Don will review our third-quarter 2015 results and various other matters followed by a Q&A session. Consistent with prior calls we are going to be sticking with just one question per caller.

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 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 will now turn the call over to our Chairman and CEO John Lundgren.

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

Thanks, Greg. Good morning everybody.

We are fortunate to be in a position to report another healthy operational quarter featuring strong organic growth as well as margin expansion. As you saw in the press release organic growth was 6% offset by currency which was a negative 8% and as a consequence net sales were down 2% as the foreign exchange headwinds we've talked about on past goals continue at historically high levels.

This was the fifth consecutive quarter of organic growth at or above 6% for the Company on a combined basis with impressive growth once again from the Tools & Storage business, 9%. Jim will give you a lot more segment detail in just a minute.

Our operating margin rate expanded to a post-merger record of 14.8% which is 70 basis points ahead of third-quarter 2014. And we attribute this to volume with the sharp cost focus, price realization in both developed and emerging markets and commodity deflation that together deliver robust operating leverage despite the $70 million in foreign currency pressure during the quarter. And we opportunistically repurchased about $200 million worth of shares within the quarter capitalizing on the recent US equity market declines.

So the combination of organic growth and the margin expansion led to third-quarter fully diluted EPS of $1.55 which was up 1% versus prior year as the strong operational performance more than offset tax and restructuring headwinds. Specifically the third-quarter tax rate that Don will talk about of 24.5% was 540 basis points higher than the prior year while restructuring charges in the quarter were approximately $14 million higher than the third quarter 2014. So the restructuring charges were about a $0.07 EPS headwind during the quarter.

As a consequence of our third-quarter performance and our outlook for the fourth quarter, we're increasing 2015 full-year GAAP EPS guidance range to $5.80 to $5.95 and that's up from our prior guidance of $5.70 to $5.90. So up 8% to 11% versus the prior year.

Not surprisingly I'm just really pleased with our organization's demonstrable agility in delivering both organic growth and operating leverage in such a dynamic operating environment. Organic growth remained strong but diving just a little bit deeper into the sources of our growth it was broad-based. Volume grew 5% and was aided by 100 basis points of price realization from a combination of efforts to combat the currency headwinds in many of our markets overseas and the implementation of surgical pricing actions domestically, resulting in a total of 6% organic growth for the quarter.

As already mentioned the foreign-exchange headwinds remain severe and they detracted 8 percentage points from our performance during the quarter. All geographies grew mid single digits with the US leading the pack and Europe growing well above market rates. Our emerging market group and the rest of the world also posted solid growth despite doing no business in Venezuela and softness in Russia, China and Australia.

Interestingly, Japan grew 8% driven by strong Stanley Engineered Fastening performance in the automotive markets.

Let's take a closer look at the segments. And Jim is going to walk you through that in a lot more detail.

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

Okay, thank you, John. I will start with Tools & Storage. It was another banner quarter for the team and their strong momentum business.

Revenue was up 2% while operating margin grew 8%. We once again set a post-merger record with a 16.7% operating margin rate, demonstrating impressive leverage. Gains resulted from volume-related incrementals, modestly positive price, variable cost productivity, continued tight SG&A cost management and some benefit from input price reductions, the combination of which more than offset severe currency headwinds.

Organic growth remained strong, up 9% overcoming a 9% comp and a noteworthy fifth quarter in a row at or above that 9% growth level. All regions contributed with strong performances as North America was up 11%, Europe was up 7% and emerging markets up 6%. Organic strength was prevalent across the global product lines with professional power tools up 9%, consumer power tools up 12%, accessories up 9% and hand tools and storage up 8%.

All categories benefited from strong customer level and new product commercial execution. Encouragingly, this overall performance shows that the Tools & Storage growth and innovation machine can continue to be successful in the face of tougher comps. The combination of the launch of our DeWalt outdoor line as well as other enhanced products in conjunction with more normal weather patterns this year resulted in the successful outdoor season that was up double digits for the quarter as well as year to date.

POS was again robust across the channels with major big-box customers in the US continuing their recent strength. Aggregate weeks on hand at retail is in a good place in line with historical levels. The US hardware lumber store, STAFDA and online channels were again very strong as construction markets benefited from growth in end-user demand and our own commercial execution took that a step further.

Mac Tools growth continued at impressive levels continuing to outpace the healthy North American automotive aftermarket on the strength of new product and a growing franchisee base. Not surprisingly we did experience softness in our US industrial markets which was directly attributable to the slowdown in oil and gas and mining end markets. Europe continued with its impressive organic growth and commercial excellence, averaging 7% growth over the last 10 quarters in a flattish market.

The share gains in the quarter have been broad with almost all markets showing a positive performance. The stream of new innovative products, adding new points of distribution and leveraging our stable of iconic brands, is a winning model that continues to reinforce our position as the world leader in Tools & Storage.

Emerging market organic growth was again encouraging at 6% as a double-digit performance in Latin America, the Middle East and Southeast Asia more than offset steep declines in Russia and a weak performance in China. The midprice point product rollout led by Stanley branded power tools continued to be timely and effective as end-users tend to be more value oriented in economies under economic duress. Clearly the scale, maturity and depth of our emerging market team in conjunction with this important initiative continues to bolster our organic growth and overall developing market performance in a more than challenging and volatile environment.

I would like to take just a moment to recognize our global Tools & Storage management team in both the developed and developing markets. The results speak for themselves: organic growth averaging 10% over the last five quarters, margins up 130 basis points year to date and at record levels despite about 150 points of FX pressure expected for the year.

SFS 2.0 is clearly enabling strong customer execution: outsized organic growth, margin expansion and over nine working capital turns. Some people have the perception that we are simply riding the US construction and DIY wave and we are to an extent. However, only about 40% of the global tools business benefits from that.

What we are clearly seeing is the manifestation of a performance culture grounded in SFS, second- and third-order benefits from the Stanley Black & Decker merger and the potential of the world's leading Tools & Storage franchise. What is exciting is that there is even more opportunity ahead as the team takes SFS 2.0 to the next level which we will begin to see in 2016.

Now moving to Security this was clearly a quarter of advancement for Security, demonstrating the operational progress that we are looking for as we pursue our multiyear plan to transform the business. Execution within Europe was outstanding and both the North American electronics and mechanical locks businesses took encouraging steps forward.

Europe again had a long list of accomplishments, including 4% organic growth, another double-digit order rate performance attrition rates within their target zone and operating margin which improved versus prior year for the fourth consecutive quarter and is now in the high single digits.

Commercial execution exhibited good breadth with organic growth achieved in all major geographic markets and signs that we are beginning to move the market share needle into positive territory. In recent quarters our European management team has demonstrated the winning spirit that comes with consistently delivering organic growth and profitability commitments while winning in the marketplace.

The US mechanical lock business also showed progress with 4% organic growth and improving profitability. Our management team remains focused on specification writing, revitalizing product lines through innovation and driving commercial excellence.

North American electronic security had a mixed quarter with more positives than negatives. On the plus side there was sequential margin expansion, operational stability and financial predictability. On the other side of the ledger an organic revenue decline.

While we continue to improve field operational performance, increase order rates and grow a healthy backlog, the opportunity to deliver growth and margin expansion is there in coming quarters.

In Security's relatively small emerging market domain significant softness in China cut into overall segment organic growth and profitability once again, muting some of the gains across the other businesses.

Now turning to Industrial. Industrial delivered another steady performance from Engineered Fastening and weathered market-related declines within Infrastructure. The net result was a 7% decrease in revenue as flat organic growth was more than offset by 7 points of negative currency.

Margins were up modestly as volume leverage in Engineered Fastening, tight cost controls and pricing more than offset the negative impact of foreign exchange and organic declines in the Infrastructure businesses. Engineered Fastening posted 3% organic growth led by double-digit performances, or double-digit performance in automotive, once again outpacing global light vehicle production which was relatively flat in the quarter.

Additionally we saw solid growth within electronics. This growth offset lower North America Industrial sales tied to weakening market conditions. All in all it was an impressive quarter of organic growth and margin expansion for Engineered Fastening despite the translational currency headwinds experienced within the business.

Infrastructure which includes Oil & Gas and Hydraulics was down 10%, in line with our expectations. Oil & Gas was down 7% as signs of life in the onshore North American market were not enough to offset continued declines in global onshore and offshore pipeline activity. Growth in Hydraulics was down 17% as volume in our demolition shares is correlated to pricing levels in the scrap steel market.

In summary, it was a solid operational performance by the Industrial teams, holding organic growth flat and expanding the operating margin rate despite soft infrastructure and global industrial markets as well as a significant currency drag.

So as we assess this quarter's performance in the aggregate, it represents another strong quarter for the overall Company with 6% organic growth and record operating margin levels that expanded 70 basis points despite approximately 150 basis points of currency headwinds. We are now on track to grow EPS 8% to 11% in 2015 despite friction from external obstacles including the strong dollar and dynamic end markets.

We are also in good shape for 2016. Our balance sheet is solid and at current exchange rates our FX headwinds will begin to decrease and we have a series of growth and margin-enhancing initiatives both underway and planned.

We also have a solid M&A pipeline and expect to resume our inorganic growth activities in a measured but meaningful way in the near future. We look forward to finishing 2015 at our upgraded EPS guidance levels and entering 2016 with a viable roadmap for revenue, cash flow and EPS growth.

Thank you. And I'll now turn it over to Don Allan.

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

Thank you, Jim. I'd like to begin with our third-quarter and year-to-date free cash flow performance.

For the third quarter free cash flow was $171 million which was down modestly from last year's results. This brings the year-to-date performance to $174 million.

The lower year-to-date results compared to the prior year is mainly explained by higher inventory levels needed in the summer and the fall of 2015 which were required to service the increased levels of organic growth we are experiencing, primarily within the Tools & Storage business.

The core SFS principles require agility to respond when business conditions change such as the strong organic growth we have experienced recently. SFS has enabled us to reach working capital and asset efficiency levels that are considered world-class compared to our industrial and security peers while being agile to changing market conditions to ensure we meet our customers' needs.

We expect by the end of 2015 we will deliver approximately a one-half working capital turn improvement versus the prior year and achieve turns within the range of 9.5 to 9.7 times which will demonstrate another step closer towards achieving our goal of 10 working capital turns. However, given our strong organic growth performance in 2015 of 6% the one-half working capital turn improvement will not translate into a cash flow benefit for the full year of 2015 but instead will result in a modest cash outflow. This is one of the benefits of great strong organic growth as it begins to become a bit of a pressure to your cash flow.

One other item of note related to cash flow, the improvement of approximately 3 turns from 6.4 turns in Q3 to the end of the year is heavily influenced by the normal Tools & Storage seasonality. For those of you who have followed our business for many years, you know that this fourth-quarter Tools & Storage seasonality dynamic is a regular occurrence given the timing of sales and shipments as they occur within the quarter. This outstanding working capital result combined with capital expenditure control and our improved earnings outlook will result in the Company delivering free cash flow approaching $1 billion in 2015.

As John mentioned during the quarter we also executed opportunistic share repurchases of $200 million.

This brings our cumulative total share actions to the equivalent of $1.2 billion in the last 12 months. As we reviewed during our Investor Day in May you should expect us to return over time to a capital allocation of approximately 50% of our free cash flow being deployed to M&A and the other 50% to our shareholders via dividends and the occasional opportunistic share repurchase.

Let's move to the next page and our updated 2015 outlook. As indicated by John earlier and Jim we are increasing the 2015 EPS range to $5.80 to $5.95 versus the previous range of $5.70 to $5.90. We are able to raise our outlook primarily due to strong business performance across several areas of the Company driven by commodity deflation and cost control.

In particular we are starting to see stronger than initially expected benefits from steel, resin and other base metals that manifest themselves in our income statement's results. However, these benefits are partially offset by foreign-exchange headwinds that are now expected to be at the high end of our previous $200 million to $220 million range when you use current rates.

Most of that impact is related to the weakening of the Brazilian real over the last two or three months. The net result of these changes is $0.07 to $0.08 increased to our midpoint outlook range that I just provided.

Moving to the right side of the page and a little bit more detail on the segments, first let's start with Tools & Storage. We continue to expect high single-digit organic revenue growth within Tools & Storage. This is slightly better than compared to our July outlook.

We also expect solid operating margin rate expansion year over year in the segment due to volume leverage, cost actions, price and commodity deflation I just mentioned which will more than offset the impact of currency.

Security remains on track with the forecast we provided in the last quarter's guidance. Margins for the full year are expected to be generally consistent with the prior year on relatively flat organic revenue.

Industrial will continue to benefit from the momentum in our Engineered Fastening's electronics and automotive businesses which will be modestly offset by slow growth and/or pressure in some of the general industrial markets and infrastructure that Jim touched on. However, this still has us on a path for low to mid single-digit organic growth for the year with a solid operating margin performance.

In summary, our revised EPS guidance range demonstrates the strong year-to-date performance across much of the Company which means we are now on track for 8% to 11% EPS growth despite currency headwinds of approximately $220 million or $1.10 of EPS.

Before leaving this page I would like to make a few comments regarding 2016. While it is premature to get into a lot of detail for 2016 the current exchange rates will result in an approximately $100 million headwind. This is related to continued devaluations of various currencies including the Canadian dollar and the Brazilian real versus the US dollar as well as the impact of our 2015 transactional foreign-exchange hedges rolling off next year.

Similar to what we did in 2015, we are proactively identifying cost reductions, aggressively pursuing commodity deflation and other pricing opportunities to partially mitigate this impact and will position us to demonstrate continued operating leverage in 2016 as well as reasonable earnings growth.

So let's summarize the presentation portion of our call today. We delivered a very strong third-quarter performance and here are some of the highlights.

We are very pleased with another quarter of strong organic growth, our fifth in a row at or above 6%. The proactive tight cost controls and surgical price actions across the entire Company enables excellent third-quarter operating leverage in the face of $70 million of currency headwinds.

The third item is the progress continues with Security's multiyear transformation with sequential improvement across most of the operations and we were very pleased with the result. We were also able to execute additional share repurchases in the third quarter as I mentioned, bringing the total share count actions we have taken since the start of the fourth quarter of 2014 to $1.2 billion.

As we communicated during our Investor Day in May our focus in 2015 and beyond will be on leveraging our world-class franchises and brands, strong free cash flow generation and continued shareholder friendly capital allocation. This continues to manifest itself in our focus on accelerating organic growth through SFS 2.0 while supplementing that growth with acquisitions, advancing Security's multiyear transformation to achieve consistent low single-digit organic growth and 15% profitability by 2018. Also continuing our disciplined approach to cost and pricing actions to ensure we have annual operating leverage as we grow.

Finally, an ongoing focus on working capital turns. We believe this approach will help position our Company to continue our strong performance trend and achieve our long-term financial objectives.

Thank you and that concludes the presentation portion of our call. Now let's move to Q&A.

Greg Waybright - *Stanley Black & Decker, Inc. - VP, Investor & Government Relations*

Great, thanks Don. Stephanie, we can now open a call to Q&A please.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Rich Kwas, Wells Fargo Securities.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Hi, good morning everyone. I'm going to squeeze in two questions here. But Jim, or John, could you comment on price as you start to look at 2016.

With the deflationary environment a lot of companies are starting to struggle in terms of pushing through price. I'd like to get your views on that.

Then in terms of the near term on Industrial how you feel about the landscape right now? There are some pressures in the environment. Have you baked in some cushion around Industrial and the landscape here as we move out the next few months? Thanks.

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

Don is going to give you the view on price going forward to the extent we're going to talk about it for 2016. And then Jim I think can give you a little deeper dive on Industrial and our thoughts.

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

Pricing I think it's a couple of dynamics. One is certainly we've been able to achieve positive pricing benefits because of some of the negative foreign-exchange impact we've had in emerging markets in particular and even a little bit in our European regions as well. So as we import both our products into those particular regions and we are impacted negatively by foreign currency we obviously try to recoup as much of that as possible through pricing actions in the local markets.

With us having a continued headwind going into 2016 we will continue to be prudent about our approach in that area and go after specific price actions where it makes sense given the different dynamics in those markets. So we do think there will be an ability to gain some price in emerging markets as a result of that pressure from foreign currency.

In more developed markets like the United States or even Europe where we're manufacturing product and selling it within the region, pricing will continue to be an area that we stay very focused on. We've been heavily focused on specific surgical pricing actions in the last year and a half to two years in those developed markets.

We don't see any reason for that to change. I think the commodity deflation impact will be an area that we have to watch closely. It impacts certain types of products and it doesn't impact other products quite as much and as I said being surgical allows you to evaluate those types of decisions.

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

Talking about the three pieces, obviously Rich you are aware that Stanley Engineered Fastening is the overwhelming majority of our industrial segment but they really are responding to some very different market dynamics.

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

Yes, I think when you talk about Industrial it always boils down to subsegments and both geographically and also just subsegments within Industrial categories. And I think what we see right now in the North American market is a dichotomy between some of the more difficult end market such as oil and gas, mining and ag in particular and then we see continued I won't call it buoyancy but maybe continued perseverance in the automotive market.

So while automotive kind of chugs on I think that's driven largely by the resurgence in consumer and also the aging fleet. So automotive is very important to Engineered Fastening, about 40% of its revenues or so. And as long as automotive is healthy that particular part of the business is going to be fairly healthy.

Then of course electronics is the other big part of Engineered Fastening, another big part and that continues to be strong as well. Then the general kind of MRO related Industrial is a function of the accumulation of the subsegments and that is a little bit on the weak side right now in North America. You can see it from some of the results of the distributors that have actually come out.

So a mixed bag in North America. We don't see it going negative at this point. It's flattish and may be slightly up or slightly down but kind of hovering around flattish.

Then Europe, Europe has been challenged in that flattish kind of way for a long time and we see a little bit of negative drag in Europe and nothing catastrophic at this point. I think the weak euro as much as the strong dollar has hurt exports in the US. The weak euro tends to have the potential to maybe boost industrials in Europe a little bit.

So I think on balance we do see some pressure in Industrial and we have factored that into our thought process. But we don't see recessionary conditions, although industrial production is relatively weak in the aggregate right now.

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

The only thing I'd add, Rich, and we'll move on when Jim talked about the markets, the North American markets in our subsegments he mentioned obviously oil and gas, mining, ag and the relatively depressed prices in the scrap steel market has had an impact on our Hydraulics business. Of course demolition as you know is a very large part of that.

So we've got those headwinds in a couple of our smaller businesses but a modestly healthy environment in Engineered Fastening both domestically and abroad. I mentioned the bright spot is Japan for us which is quite encouraging and the business is doing quite well.

Operator

Michael Rehaut, JPMorgan.

Michael Rehaut - *JPMorgan - Analyst*

Thanks, good morning everyone. The question I had was just regarding getting a little bit more granularity with the adjustments to the full-year guidance. If you take the midpoint of the prior FX headwind to where you are expecting today it doesn't seem like it's that much more, maybe $10 million or $15 million or $10 million from the midpoint.

So I just want to understand versus three months ago what were the biggest drivers of those? And then conversely in terms of the upside stronger business performance combined with better commodity deflation, if you think of the $10 million incremental headwind to get to the guidance raise, you're talking about maybe another $15 million or I'm sorry $25 million of positive roughly speaking. So if that math is right $25 million or

$30 million of incremental positive, how does that break down between the stronger business performance and the commodity deflation and more specifically where within the business are you seeing that better performance and what's the bigger weight?

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

Rank has its privileges and I'm going to let Don try to tackle that one. There is a lot of moving pieces, Mike, but I think Don can cut it, tie a little bit of a bow on it for you.

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

Sure. Your math is actually pretty close. So as you think about us raising our midpoint by about $0.07 or $0.08 of EPS yes, we probably have about $10 million of new FX pressure.

As I said we're at the higher end of that range. That's about $0.05 of EPS.

And then you have about $25 million or so of positive impact from commodity deflation and other indirect cost controls. And the net of those two items gets you basically to $0.07 and $0.08.

Operator

Jeremie Capron, CLSA.

Jeremie Capron - *CLSA - Analyst*

Thanks, good morning. I wanted to focus a little bit on the Tools & Storage segment. Margins were very strong, I understand the good volume leverage here, but it looks like we're coming in at the high-end of that range that you've talked about in the past as being sort of the cyclical high margins that we could expect from his business.

Any change in your view here given that at this point you still have the 150 points of ForEx pressure? In those margins should we envision margins continuing to trend up into next year as long as volumes go up?

And the other question, the follow-up on this is I understand you have very strong share gains across regions. I just wanted to get a better sense of what you see in terms of the underlying demand trends in North America in particular.

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

Sure. This is Jim. When we think about margins and margins through the cycle we don't necessarily let the cycle drive the margins per se.

We tend to be much more proactive about it. And at the down part of the cycle we're taking out cost at a very healthy pace and as we enjoy the ride up the cycle, we don't back off in terms of some of the things that we do to maintain the upward pressure, everything we can do to maintain the upward pressure on margins.

So I think the potential for what you're calling the peak cycle margin rate is quite high. And I think evidence of that is if this whole FX headwind hadn't occurred we would be at record margins for the Company and the tool business.

So the things that we do are things like continuous productivity, 3% to 4% cost productivity every year. We have a very, very surgical and data-driven pricing program in this Company which goes across all the businesses including the tool business where we constantly are improving our subject matter expertise and our analytics in pricing and looking at price volume trade-offs and making sure that we're optimizing our margins and our overall margin in that regard.

Then we have designed to value which is a more programmatic approach to driving cost out of products. In the design cycle we have a simplification and complexity reduction program which again drives cost out of the products and we have mix management. We are doing everything that we know how to do to drive margins up.

And where that limit is we don't know but we constantly try to drive them up. So I think that's the way we think about it.

As far as the share picture in various geographies in the tool business I have to say that I don't think there's any region in the world except with the possible exception of China where we are not gaining share. This business has implemented a commercial excellence initiative which has taken the strength of Stanley Black & Decker's scale, its brands, its products, its innovation and it is driving that across all geographies in a very aggressive way and it's been very successful and we expect it to continue to do so.

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

And Jeremie, it's John. Just to add to that both in terms of our drive for margins and share gain, more from a qualitative perspective but I think it's demonstrable.

In the past two months we've been named category specific vendor of the year by our two largest customers. Never before at least in our history, I've been here 11 years and Jim and Don 15, have we achieved such coveted and prestigious recognition from our two largest customers in the same year.

I think if nothing else or just anecdotally this is a tribute to the strength of our brands, the strength of the programs and the commercial execution that Jim was talking about and obviously those kinds of things are leading to share gain. We're pleased with that.

Operator

Jeffrey Sprague, Vertical Research.

Jeffrey Sprague - *Vertical Research - Analyst*

Thank you. Good morning everyone. John, you briefly just mentioned China and I just have a question overall thinking about the dynamics and the EMs in Tools & Storage specifically.

A very strong performance that you characterized with strong Latin America offsetting a weaker Russia and China. It would seem difficult for Latin America to continue to carry that ball with what's going on in Brazil, etc. Just wondering if you could kind of give us a little bit more granular lay of the land on how you think those things play out.

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

Sure, Jeff. Very fair. To give you some numbers because they are all over the place.

Latin America, what we call our Latin American group organically grew 13%. Brazil which is the largest by far market grew 4% organically but obviously we're suffering some huge currency headwinds that Don talked about. But we have smaller countries, Venezuela as I say, where we've done zero business essentially for about the last six quarters.

But we had good performance in Mexico, good performance in Colombia. Brazil as I said up low single digits which gave us low double-digit growth in Latin America. Country specific, they represent a small percentage of volume but Russia was down 30%, China was down 28%.

We think that's not inconsistent with the markets in general. The silver lining in the clouds for us particularly in China is the expansion of our midprice point product offering locally produced by a subsidiary that we control.

We think that in another itself is going to help us a lot. But we're working off some high comps.

The bad news is we're down 25% to 30% in both Russia and China. The good news is those are very small markets and a small base. So a couple -- $3 million, $4 million of improvement will bring us back to where we were.

What we're doing about it I think the simplest way to describe it we aren't withdrawing, we aren't cutting back, we've stopped adding feet on the street and variable cost resources at the pace we were adding them. But we haven't cut anything and we're just reallocating resources within our emerging market group Asia and to a lesser extent Latin America because we just think those are still huge economies, 45% or 46% of our business is still outside the US, that includes Europe of course, and we're not going to withdraw our support for those markets.

So long answer to a simple question but I think the huge volatility in certain countries gives you a flavor for how we're approaching it. It's much more question we're reallocating resources as opposed to cutting them because we're in these markets for the long haul.

Operator

Michael Dahl, Credit Suisse.

Michael Dahl - *Credit Suisse - Analyst*

Hi, thanks for taking my question. I wanted to focus on the Security segment. You've got kind of diverging trends here.

On the one hand the previous problem area in terms of Europe is improving and seeing accelerating organic growth and now it seems like you're seeing some deceleration in North America and emerging markets I guess on the electronic side in particular. So just curious as you look out to obviously you've outlined a path to what you need to see from this overall business over the next year.

How are these trends playing into that? Are you more or less positive on the positioning of the business as you see it today versus how you were thinking about it three or six months ago?

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

Sure. Fair question. Don will give you a little detail but I guess from the top of the house I can say we feel as good or better about these businesses as we have in the past.

You talked about Europe, they are delivering on their commitments which pleases us and pleases the folks there. We think we have the right people in the right chairs and we think we understand what the issues are within North American Security. Don has been spending a lot of time with that team so let me have him give you a little more granularity.

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

Thanks, John. So what John said is exactly correct and we're really pleased and Jim went through it in a lot of detail in his presentation around the European performance, how it continues to improve demonstrating a short stretch of time here with consistent organic growth, sequential improvement in operating margin rate, all the things that we talked about a year ago that we wanted to accomplish with that business where we're seeing them really get traction in all those areas.

In North America I wouldn't say that we feel like we're losing traction and are slowing down. We definitely know that we had a little bit of a blip on the radar in the second quarter of this year because of a large installation that completed itself. It didn't repeat as you can see in the third quarter because the third quarter bounced back to our expectations, they are actually slightly better than our expectations around profitability.

And we continue to deal with an evolving and changing environment related to our vertical selling solution, specifically targeting two verticals, retail and healthcare is an area that's really concentrated in helping the business grow. The positive in North America that I see is that backlog continues to grow and the order rates are double digit and these are trends that we see now for two or three quarters which is positioning us well for next year to demonstrate some organic growth in North America in electronic security and mechanical security for that matter.

So the last piece is China. Overall emerging markets are relatively small for the Security business and outside of China it is doing relatively well. But in China because of the economic circumstances, market conditions we've definitely seen some of the retrenching revenue declines the John mentioned in China a few minutes ago of double-digit declines and that's been significant.

We think that's more market related. It's not a big part of the business. Like everyone else I think we all think China will begin to gradually get back on track at some point in the next two to three quarters probably, but so we're not overly concerned about that. So our focus now is continued execution improvement in Europe, continued execution improvement in North America and really hunker down in emerging markets, get through this period of time in China and then begin to demonstrate growth as we come out of that.

Operator

Tim Wojs, Baird.

Tim Wojs - *Robert W. Baird & Company, Inc. - Analyst*

Hey guys, good job again in a tough environment. I just had a bigger picture question on Tools.

What inning do you think we're in around some of the adoption of some of the new technology development that's been going on whether it's brushless or just improved battery performance? And I guess would you characterize this as maybe a technology step function that's similar to what lithium-ion was a few years ago, was several years ago?

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

I would say Tim it's a really good question and I would say no. Lithium-ion if you think about it relative to NiCad it was a better mousetrap, more power, longer runtimes, better for the environment and the only issue was cost. And like any technological breakthrough when you can get the cost in line it is going to displace its predecessor.

What we're seeing now and I don't think it's a step function. I think the answer to your question which is a very fair one and it's only one person's opinion that you're getting. That being said, the leverage for us is going to come from what I think we do best.

We weren't the inventors of brushless. We obviously didn't invent it and we were a slow follower on the application of lithium-ion and things of that nature.

Where I believe we've excelled and I give tremendous credit to our global tools and storage team both in the product development perspective, commercial execution, etc., is just the application of all of those technologies. The application of brushless, lithium-ion, the way we've been able to get more power, more runtime combined with the DeWalt brand, good programs to support it, those are all I would argue incremental as opposed to step functions. And that's where our success has come the last two or three years.

Is there more on the horizon? Yes I think we can see we're cautiously optimistic about what our team has in the pipeline in terms of further advancements of those existing technologies but I don't see anything in the application of those technologies.

But I don't see another lithium-ion if you will breakthrough per se in the foreseeable future. But that doesn't mean we're not going to push those hard and get more than our fair share of the market growth by applying the technologies.

Operator

Mike Wood, Macquarie.

Mike Wood - *Macquarie Research - Analyst*

Hi, thanks for taking my question. Can you give us some color in terms of the North America vertical products and Security, just what the lifecycle on the margins look like relative to your more typical products there? If you could just differentiate maybe on the install, would we expect lighter, and is that what we're seeing now and does that become more of a tailwind as you get more to recurring with the vertical products?

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

Yes, I'll take that one, Mike. You know, the verticals that we're really concentrating on right now are retail and healthcare. And as you know the idea of the vertical selling solution is to really create a solution that offers much more than just Security to our customers.

Security is certainly a core component of the solution but are there other things that we can do such as in retail where we provide certain information and data based on traffic flow in and out of the stores, correlating that with POS, etc. In healthcare we're looking at helping productivity within the healthcare environment of the nurses and doctors and offering solutions in that area to help the customer save, reduce cost or save money.

And so the model is really to bring forth those types of solutions that give more value and that does that translate into more beyond the installation into certain types of recurring revenue streams. And that's really the intention of it.

At this stage it's still early development around that but as we get deeper into the verticals in particularly the two that I just mentioned I do believe that certain recurring revenue streams will evolve from those types of solutions. So I think that's something you continue to watch and monitor. It's an area of focus as part of our strategy.

Operator

Robert Barry, Susquehanna.

Robert Barry - *Susquehanna Financial Group - Analyst*

Hey guys, good morning. Just a quick housekeeping first. I wanted to clarify those growth rates John was giving earlier on the emerging markets if that was for just Tools or the total Company.

But then my question was really on SG&A, 21.5% of sales, very good performance, actually it looks like a record at least in recent history. Just wanted to unpack a little more what's driving that, how much is structural and how should we be modeling SG&A going forward? Thank you.

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

I will clarify the first one. The numbers I gave, the growth rates or lack thereof in some of the emerging markets were total Company. That being said with the exception of certain Asian markets that is overwhelmingly global Tools & Storage.

As Don mentioned Singapore, China, some meaningful Security business 20% of our total in those markets. But they were total Company numbers which were overwhelmingly Tools & Storage. Don, do you want to talk about SG&A?

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

Sure. So very pleased with the SG&A as a percentage of revenue in Q3 at 21.5% or in that category. But for the year we do expect to be similar around 22.3%, 22.4% for the total year.

We do have some additional costs that do creep into the system for lack of a better word in the fourth quarter related to some of the promotional activities we do and in-store activities around the holidays, that will likely make that number creep up a little bit in the fourth quarter versus the third quarter. But we are definitely seeing another step change in this particular area in 2015.

So in 2014 were close to 23% as a percentage of revenue and when we end the year we will be somewhere between 22.2% and 22.4% by the time we close out the year. So that's a significant improvement.

Part of that is what we've been doing for the last few years around indirect cost focus and how do we become more efficient, how do we drive more benefits and productivity in the use of those particular dollars. And then also we've had a little bit of benefit although it's not huge from consolidating our CDIY and IAR businesses into the new business called Tools & Storage.

So those things together have really helped leverage that objective. And I do think we're at a point now where we can continue to drive that down further.

As you know we talked about it I specifically talked about it at Investor Day and we think we can get this number down even further through functional transformation as well as taking some of those savings that we achieved and reinvesting things like digital excellence, commercial excellence, breakthrough innovation, etc. But the net result is really to drive our operating margins to 16% and a lot of that is going to come from what we're trying to do in SG&A along the way.

Operator

Liam Burke, Wunderlich.

Liam Burke - *Wunderlich - Analyst*

Yes, thank you, good morning. The Black & Decker brand has been fairly successful in your mid-price point overseas but how is the Black & Decker brand being positioned domestically?

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

The Black & Decker brand domestically, I have got to bifurcate, Liam, but from the perspective of tools it's overwhelmingly domestically a DIY brand and its performing really, really well. You will find it in the home centers but you'll also find it in big boxes like Target, like Wal-Mart and places like that where it's very well perceived.

You know, a large outlet for the Black & Decker brand which I'm sure you are aware of but I need to be careful to distinguish it's in the home products both in the US and Europe. The overwhelming majority of these products are licensed as I'm sure you know and we obviously achieve, receive a royalty for the use of that brand on products designed for use in the home and primarily in the kitchen secondarily. So it's important to bifurcate.

But in both cases it's DIY, nonprofessional but premium quality for folks who are doing it, not for a living but folks who are serious about the product they purchased.

Operator

David MacGregor, Longbow Research.

David MacGregor - *Longbow Research - Analyst*

Yes, good morning everyone. Congratulations on a great quarter.

I guess a question on Engineered Fasteners and just the automotive business in particular. And I realize you are not talking about 2016 yet but automotive is a business where maybe there is a little more forward visibility because of platforms. And I am just wondering about your content per vehicle and how you expect that to grow in 2016, if you can talk about that.

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

Well, our strategy is always to grow our content per vehicle and as you know we're selling solutions. We're selling the equipment or the systems as well as the consumables that go with it.

I am not going to get ahead of myself or ourselves or the business particularly as it relates to anything proprietary with our customers. But our strategy is always to increase the content per vehicle and that in and of itself is a great source of growth and it's why we've been able to grow in some cases two and three times the rate of light vehicle production.

And what's playing to our strength there, and I know you understand our business very well, what's playing to our strength there is the lighter the vehicles become, particularly aluminum, it plays to our strength. When you can't weld for obvious technical reasons that advantage is systems such as ours. So we're looking to grow that content and that absolutely is a source of growth, all things being equal, above and beyond the growth of light vehicle production.

Operator

That does conclude the Q&A session. I will now turn the call back over to Greg Waybright for closing remarks.

Greg Waybright - *Stanley Black & Decker, Inc. - VP, Investor & Government Relations*

Stephanie, thank you. We'd like to thank everyone again for calling in this morning and for your participation on the call.

And obviously please contact me if you have any further questions. Thank you.

Operator

Thank you. Ladies and gentlemen, that does conclude today's conference. You may all disconnect and everyone have a great day.