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SWK - Q4 and FY 2013 Stanley Black & Decker, Inc. Earnings Conference Call

EVENT DATE/TIME: JANUARY 24, 2014 / 1:00PM GMT

OVERVIEW:

SWK reported 2013 GAAP EPS of $3.26 and 4Q13 GAAP EPS of $0.41. Expects 2014 GAAP EPS to be $5.18-5.38 and 1Q14 EPS to be roughly $0.95-0.98.

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PRESENTATION

Operator

Welcome to the fourth quarter and full year 2013 Stanley Black & Decker, Inc. earnings conference call. My name is Lorraine 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 and Government Relations, Greg Waybright. Mr. Waybright you may begin.

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

Thank you, Lorraine. Good morning, everyone, and thank you for joining us for Stanley Black & Decker's fourth quarter and full year 2013 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 app. A replay of this morning's call will also be available beginning at 2:00 PM today. The replay number and the access code are in our press release. This morning John and Don will review Stanley's fourth-quarter and full-year 2013 results and various other matters, followed by a Q&A session.

As we normally do, we will be making some forward-looking statements during the call. Such statements are based on assumptions of future events that may not prove to be accurate, and, as such, they involve risk and uncertainty. It's therefore possible that actual results may differ materially from any forward-looking statements that we might make today. We direct you to the cautionary statements in the 8-K that we filed with our press release and in our most recent 34 Act filing.

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

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

Thanks, Greg. And good morning, everybody. Normally, for those of you who follow us know, normally I would kick this off and turn it over to Jim to deep dive into some of the segments.

Jim's with us this morning but he's recovering from a bad case of the flu and a modest case of laryngitis. So Don and I are going to share the formal part of the presentation. Jim is here and we're going to try to save his voice for Q&A and get him back on the field in full force by Monday. Don?

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

Thanks, John. Let's just start with a summary of our fourth-quarter and full-year 2013 results. The fourth-quarter revenues increased 9%, which were driven by a 4% organic growth performance. And the majority of the difference between the 4% and the 9% was the addition of Infastech, as we continued to see a good performance in that business in the first year of acquisition.

The fourth-quarter diluted EPS was $1.32 before M&A and other restructuring charges, so within our implied guidance range of $1.24 to $1.34, the higher end of the range. And then the GAAP EPS was $0.41 as we recorded several additional restructuring charges that we communicated in December related to some cost actions across all our businesses to improve our operating leverage.

CDIY and Industrial posted very compelling top- and bottom-line growth performances, with CDIY achieving a solid, robust organic growth of 6% at a 14.6% operating margin rate. Industrial posted over 16% operating margin rate, and an 8% organic growth story as they continued to see gains across all their businesses.

Our Security recovery is underway. And we delivered margins that were consistent with our expectations, which were relatively consistent with the third quarter at 12.2%. The full-year results for 2013 were solid from a revenue perspective, with revenues being up 8%, 3% organic growth, which was given primarily our CDIY and Industrial businesses which saw 4% and 5% organic growth, respectively.

Diluted EPS prior to M&A charges for the year were $4.98, again at the higher end of our guidance range which was $4.90 to $5 that we provided back in October. And a GAAP EPS of $3.26.

Another positive that we saw in the fourth quarter was a very strong free cash flow performance. Our free cash know for the year before M&A payments was $854 million.

And we achieved eight working capital turns associated with that. That was slightly ahead of our expectation that we communicated in October of $800 million. And most of that outperformance was driven by a stronger working capital turn performance.

We also will be reiterating our guidance for 2014 today with a full-year range of $5.30 to $5.50 before approximately $25 million of restructuring, which will be a dramatically lower level of restructuring in 2014 versus 2013. Free cash flow is expected to be $675 million, which is inclusive of about $250 million of one-time payments. I'll provide a little more detail on that later on in the presentation. So overall, a very solid top- and bottom-line performance in our CDIY and Industrial segments, and we feel our Security recovery is under way.

I'd like to spend a few more minutes talking about our revenue performance and then I'll hand it over to John to talk about the growth initiatives in the three segments. Looking at sources of growth, in the fourth quarter I mentioned our organic growth was 4%, which is a trend that's positive, that's continued now for three quarters, where we saw second quarter organic growth performance of 5%, third quarter of 4%, and then as I mentioned fourth quarter again at 4%, for a full year equal to 3% performance. Acquisitions, primarily Infastech, contributing the 6% and then a modest negative of currency, primarily being driven in countries as Canada, Brazil and Argentina.

To the right side of the page, looking at the regional revenue performance, you can see that we continue to see a positive trend in our United States revenue performance, up 4% organically in the fourth quarter, 3% for the full year. European performance was flat for the year, up slightly, up 1% in the fourth quarter. And there's various stories within the European performance as you'll hear about from John later on, but some very healthy performances in CDIY and our Industrial segments, as we saw mid single-digit organic growth in those particular segments in the fourth quarter.

Emerging markets, as we expected, was a little slower in the fourth quarter, up 5% organically, with a solid 8% organic growth performance for the full year. Resulting in a total performance, as I mentioned, of 4% organic growth for the fourth quarter and 3% for the full year. So, we definitely feel like that our organic growth initiatives are gaining traction. And we are focused on making sure that we turn our European Security business into positive organic growth story, as well.

With that, I'll turn it over to John.

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

Thanks, Don. The organic growth initiative that Don talked about was a real focal point for us in 2013. And this chart captures some of the key highlights of those initiatives which are taking hold and, in fact, driving approximately 2 percentage points or 200 basis points of growth in 2013.

From a geographical perspective, our global emerging markets business is growing at 2.5 times the rate of the combined market average. That's the market weighted by our 2013 revenues, which reflects our higher than normal Latin American concentration.

We hired 300 new people. That included key country leaders in key sales positions, primarily feet on the street, but with the focus, again, on customers and driving growth. We dedicated SBUs and business teams versus the specific markets. And we launched approximately 300 new SKUs.

Our Tier 2 distributor expansion is progressing. We added about 1,500 new distributors.

And last but absolutely certainly not least, we're preparing for a mid-price product launch. And that will be significantly accelerated through the completed acquisition of GQ that Jim talked to you about several quarters ago. It will really allow us to make an in-market specifically designed product for that fast-growing and highly important mid price point product in the emerging markets.

Our M&A revenue synergies continued. The focus there was in CDIY where we continued to leverage some Black & Decker synergies, as well as the synergies from the Powers acquisition. Together they outperformed what we proposed as an original plan by almost two-fold in 2013.

And, as Don suggested, our Security verticals are certainly gaining traction with about $40 million of 2013 revenue attributable specifically to this activity. The order momentum is building. We've got about $100 million of annualized orders as a result of these initiatives, with the greatest success so far with our global customers in our healthcare and education verticals.

With these verticals, one of the drivers is to differentiate ourselves, and we're doing that versus competition with these unique offerings. And as a consequence, we're able to command, in most cases, a premium due to the meaningful value proposition. So, the most important point to note is these initiatives are margin accretive as a consequence.

Let's look now at some of the segments in a little bit more detail, starting with CDIY, where organic growth was up 6% with all regions delivering solid growth, 6% for the quarter, 4% for the year. North America up 5%, emerging markets 8%, and Europe 7%, consistent with total Company. This represents about half our revenue, as you know.

Organic growth was posted essentially everywhere, all SBUs reflecting market share gains, driven by both product innovation / introduction and great channel retail partnerships. And, as Don mentioned, for the total Company it's important to note in the CDIY trend 4% for the year, CDIY was flat to marginally down in the first quarter, followed sequentially by second-, third- and fourth-quarter organic growth of 6%, 5%, and 6%, respectively, leading to 4.3% for the year. So it's on a very solid path, very strong trend, and exits the year and enters 2014 in a very good place.

Looking at segment profit, it's up 7% and margin's up about 10 basis points. With the improvement reflecting both volume and productivity, and those impacts offsetting some serious foreign exchange headwinds, as well as the expense of our growth initiative investments.

Looking at organic growth in the fourth quarter by our various SBUs, a lot of positivity. Our professional power tools business is up 5%, driven by new product introductions, as well as great performance in the emerging markets. The Consumer Products group is up 6%.

Great success in Europe with steam and hand vacs. Good sell-through on North American holiday promotions. And, again, good performance in the emerging markets.

Hand tools and storage up 8%, DeWalt hand tools being a strong driver. Emerging markets and very good quarter in the UK where our business is doing well in an economy that seems to be turning the corner, which hopefully is a good, positive indicator for the rest of Europe.

And last but certainly not least, in fastening and accessories. Bostitch expansion and Powers' revenues led to 8% organic growth in the quarter. So, strong both top- and bottom-line growth in the face of currency headwinds, and a good, solid quarter for CDIY in the fourth quarter.

Moving on to Industrial, solid quarter again, delivering 27% revenue growth, of which 8% came from volume. Pricing was flat. Acquisitions, primarily Infastech, contributed 20%. And currency was a 1% negative.

The OM rate of 16.1% was strong as volume leverage was offset by the expense from the growth investments as well as foreign exchange. Looking within the segment, IAR had strong European growth. We had the Equip'Auto Fair, a very important event in Europe. We had strength in MRO and vending, as well as Mac tools.

And those positives were partially offset by weak government sales, which are normally strong in the fourth quarter, particularly in October. Greg and Dennis have fielded a lot of questions on just what is the magnitude. And, for clarity, it was about $6 million, we felt, of lost revenue, which is about 2% globally, but 4% for our North American IAR business.

And the Equip'Auto, to which I referred, is a very important event. It takes place in France but it's a European automotive and industrial tool event. Contributed about $3 million, which is about 1% globally and 4% Europe to our IAR business. So even without Equip'Auto, European IAR would have shown positive growth. And, again, another really good sign for the performance of that business in that market.

Good, strong quarter for engineered fastening. Automotive share gains leading to organic growth again for the third or fourth consecutive quarter, in excess of light vehicle production. Light vehicle production grew about 4%. We grew 5%-plus organically.

The Infastech integration is on schedule, is tracking well versus expectations. And great turnaround story in our infrastructure business. Oil and gas up over 35% organically, driven by a combination of the North American onshore growth, as well as offshore activity in the Gulf of Mexico and in Brazil.

So, good, solid quarter in Industrial. Margin rates are strong, despite the investments and some foreign currency headwinds that we'll continue to deal with through 2014. And Don will talk a little bit more about that in the outlook.

Moving on to Security. The improvement's underway. Margins were consistent with the third quarter. But I think ultimately it's helpful to separate North America and Europe because they're on very different improvement trajectories.

Going across the top of the chart, globally revenues were down 2%, 3% organically. And the segment profit was down 27% or 400 basis points.

Looking sequentially, segment operating profit of 12.2% was flat versus the third quarter, making second-half margin rate up 160 basis points versus the first half. But I think importantly, let's look inside the two different businesses. On the left, our North American and emerging market businesses were flat in terms of growth, with a strong 17.4% operating margin.

The emerging markets and automatic doors growth, which was strong, was offset by a comparison versus our fourth-quarter 2012 commercial lock distributor loading. Jim has discussed in a lot of detail the change in our operating model. I'll touch on it a little bit more in a minute.

But for perspective, in the fourth quarter it was down in SMS about 5%, which meant they were plus 1% for the year. If you adjusted for that load-in, it would be about plus 14% for the fourth quarter and about plus 11% for the year. We got the benefit a year ago, call it pipeline, so it shows up in the comps this year. But we think it was an absolutely critical change to make and the business seems to be in the right place.

The sequential operating margin rate improvement also continues in North America. Measurable improvements in field efficiency led to stronger install margins. Our backlog conversion was up 2 to 3 points.

And, as I mentioned earlier, the vertical solutions have been accretive to margin. We've shown a lot of price discipline. If we've lost any business, it's been due to price.

But we feel that we're commanding a premium for our value proposition, and we're getting it. It's demonstrated in a 265 basis point increase to 16.1%, if you look at the entire second half of the year when those programs started to gain traction.

And, as I discussed a second ago, the commercial lock transition, it is complete. The distributors have replaced the direct sales model, which was a significant change for us in the last 12 months. But we think a very important one relative to our long-term growth objectives.

Turning to Europe, volume down 8% organically, or sales down 8% organically, and a 4.3% operating margin. Lower backlog conversion and RMR attrition continued to be the issues. That being said, we had a double-digit order rate improvement in the fourth quarter.

And RMR attrition has slowed to the mid teens. It's down about 200 basis points from the level of the first half of the year and continues, we think, on the right track, albeit at a pace slower than we'd like to see it. As I'll say in a minute, our objective intermediate to long term is RMR attrition at about a 10% rate.

We've announced cost reductions to resize the business. We've applied a lot stronger centralized daily management model, which is perfectly applicable to Europe, some of the best practices from our US business. Again, improved backlog conversion efficiency and managing RMR down to 10% from the mid-teens level where it is today.

Importantly, not mentioned on the chart, our healthcare business is included in our external reporting for Security. We don't spend much time on it. It's a relatively small business but had a very solid fourth quarter in terms of its advancement against strategic objectives, revenue performance, and 11.7% operating margin. So, continuing its upward trend in a business that we continue to think could have great prospects for growth, margin and shareholder value creation in the future.

Let me turn it back to Don to talk about fourth-quarter cash flow with which we were quite pleased. And then we'll get back to an outlook and open it up to Q&A.

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

Thanks, John. So, to spend a little bit of time on the fourth-quarter free cash flow as well as the full year, you can see that our free cash flow did exceed our revised expectations. October we provided guidance of free cash flow for the full year of $800 million, as I mentioned earlier. Also embedded in that expectation was that working capital turns would probably achieve about 7.7 to 7.8 turns for the full year.

As you see, our turn performance was actually 8 working capital turns, which was a solid performance year over year, up about a half a turn versus 2012. So, where we expected in October a slight negative from working capital for the full year, we actually saw a slight positive of $13 million. That drove the vast majority of the improvement, as many of our business teams were focused on enhancing the working capital performance through making permanent long-term changes to their business, in line with the Stanley fulfillment system, and staying focused on those objectives along with achieving the right level of earnings and organic growth performance.

Overall, when you look at the GAAP performance of free cash flow, it was $500 million for 2013 versus $580 million for 2012. And we expect that number to be $675 million for 2014. To make it comparable, excluding the M&A payments in 2014, it will be $925 million versus the $854 million.

So we would expect continued modest improvement in working capital. And obviously earnings accretion, as well, associated with our EPS projections.

We believe that the free cash flow of this Company continues to be an area that we can differentiate ourselves versus other companies. And as we move away from many of the large M&A and other restructuring charges over the next two years, we will begin to approach that $1 billion objective on a GAAP basis.

So with that, I'd like to spend a few minutes reiterating the 2014 outlook. As I mentioned earlier, we expect the EPS to be $5.30 up to $5.50 of EPS before the M&A charges. On a GAAP basis we expect it to be $5.18 to $5.38. So, approximately $25 million of restructuring charges, down dramatically from the approximately $400 million we saw in 2013.

I mentioned the free cash flow projections for next year, so I won't touch on that again. Some of the assumptions within the guidance have remained consistent with what I mentioned in December. So, 4% organic growth is expected, approximately, for next year, which is relatively consistent with what we've seen over the last three quarters in our Company.

150 basis point improvement in Security margins. So, all the things that John touched on that we're seeing come to life in the North American business, and the expectation of what will occur in our European business as the year goes on would drive that improvement.

We also discussed in December some surgical cost reductions we did across our other businesses in CDIY and the Industrial segments. And then some corporate actions that will drive about $0.20 of EPS improvement year over year. And then, of course, in year two of our integration of Infastech we expect some synergies and accretion in that business that will drive about $0.10 of EPS improvement.

On the headwind side, as we mentioned in December, we do expect carryover pressure of foreign currency. And so, where we saw about $60 million of negative currency effect in 2013, primarily in the back half of the year, we would expect a very similar number to occur in the first half of 2014, which would equate to about a $0.30 negative in EPS.

The tax rate will be slightly higher versus our roughly 19.5% tax rate we saw in 2013, somewhere between 21% and 22%, as a few one-time items that occurred in 2013 we don't expect to repeat. And then a little bit higher interest and a few other costs will drive a slight negative of $0.10 to $0.15, as well.

One other item of note I want to just have people focus on is just the timing of the quarters for 2014. As usual, we do have a seasonality impact in the first quarter but it is slightly lower than normal history based on two factors.

One, that foreign exchange impact that I mentioned carrying over from the back half of 2013. And then, two, we do have a slightly higher tax rate in the first quarter this year versus the first quarter last year, as we did record approximately a $10 million benefit, one-time benefit, in the first quarter of 2013. So, as a result, we expect the first quarter to be roughly between $0.95 and $0.98 EPS.

A little bit of segment outlook to the right side of the page. We expect mid-single-digit organic growth in both our CDIY and Industrial businesses for 2014. Again, very consistent with what we've seen, especially the last two or three quarters in these businesses.

The Security business, from a revenue perspective, will be flat to maybe a modest increase, as we expect North America and emerging markets to continue to demonstrate some solid organic growth, especially as we see the organic growth initiatives become even stronger in North America. And then the European business will probably be down slightly versus prior year, as we expect to see a little bit of pressure, especially in RMR attrition in the first half of the year as we begin to see that flatten out in the back half and achieve the 10% RMR attrition rate that we'd like to see in that business going forward.

Operating margin -- we expect increases year over year in the operating margin rate for both CDIY and Industrial as we see the leverage effect of the organic volume. Of course, that's partially offset by the FX that I discussed. And we also see a benefit of some of the cost actions that we've taken that are surgical in nature. And then the operating margin rate for Security I touched on -- was 150 basis point improvement year over year.

The last thing I'll say is, as I mentioned earlier, the M&A charges go down dramatically in 2014 from a level of $400 million approximately in 2013, to $25 million in 2014. Dramatically closing the difference between US GAAP and EPS on an adjusted basis, which is one of our primary objectives for 2014.

I'd like to spend a little bit of time on the next page going through emerging markets and foreign exchange. As many of you are aware, we've had significant impact in 2013 and, as I discussed, expect some more significant impacts in the first half of 2014 related to this.

In the page we show the currency trends versus the US dollar for really the four major currencies that tend to have a significant impact on us. The first three have historically had a large impact on us since the merger. The European euro, the Canadian dollar and the Brazilian real.

The Argentinean peso has become more challenging over the last few years as that country continues to see governmental challenges and economic issues. If you look at the euro, it's been relatively flat over the last 12 months, actually a slight improvement, about 3% versus the US dollar. However, the Canadian dollar and the Brazilian real have seen 11% and 15%, respectively, devaluations versus the US dollar, with a lot of that happening since June of 2013. The Argentinean peso, approximately 40% in that same time horizon.

To give you some context on the size of the businesses in these countries so you have a sense of that, our European business is just under $3 billion, about $2.9 billion in revenue. The Canadian business is approximately $0.5 billion in revenue.

Our Brazilian business is $230 million in revenue. And our Argentinean business is $115 million in revenue. So that gives you some context of the size of the businesses, as you start to look at some of the magnitude of these changes.

Now, when we look at where does this impact our businesses. It impacts primarily our CDIY business. About 80% of these impacts go into CDIY, with the other 20% hitting our Industrial businesses, which is mostly industrial automotive repair and engineered fastening.

It's driven by the global supply chain that we've created, where we do have a lot of business that is imported into, in particular, Latin America and Canada. So, it's manufactured in other countries and imported into those regions. And, as a result, it's US dollar-based and can drive a significant currency impact when we have a shift in currency either way.

What do we do from a mitigation perspective related to that? Obviously, there's many things that we do. In Latin America and Canada we're always looking at potential for price increases with our customers as the currency moves.

To use Latin America as an example. Over the last two years, as you've seen these types of shifts, we've had numerous price increases in many of the countries over that time horizon to offset that impact.

Obviously the timing is a little different than the shift that you see related to currency. But overall we try to do our best to pass on as much as we can to the end user and our customers. We're also focused on cost controls in those particular areas.

We do look at localizing production where we have enough mass in certain countries. In the case of Brazil we do have certain levels of production down there and we continue to evaluate moving more production into that country. But we have to make sure we balance that against ensuring we have the lowest cost possible when you factor in the currency, as well.

And then last but certainly not least, in some countries we are focused on what hedging activities we can do against the currencies. In the case of Brazil and Argentina, it's very difficult to do that. It's either very cost ineffective or, in the case of Argentina, it's almost impossible to do it due to certain regulations.

The last thing I'd like to touch on is just the estimated financial impact of some of the movements of these currencies. Over the last few years I've provided you some detail on this and I'd just like to reiterate that. I already discussed what the dollar impact is for 2013 and 2014 of these movements.

But if you look at the four different currencies, you can see here that a 1% movement of the Canadian dollar has about a $3 million to $4 million annual impact in our P&L. The euro is about $1.5 million to $2.5 million with a 1% move. And then the Brazilian real is a $1.5 million to $2 million movement on an annual basis. And then you see the Argentinean peso, as well, which is a much smaller number.

This is really more for you to be aware and educated on based on how these movements can impact us both in history but also on a go-forward basis. And our guidance is predicated really on where rates are today. And we'll continue to be focused on what actions we can take, as I mentioned, in the mitigating factors as we see shifts beyond where these rates are today and how we can respond to them, to ensure that we achieve our guidance for 2014.

With that, I'd like to summarize the presentation portion of the call this morning. The Company remains committed to driving both long-term and near-term shareholder value. We discussed that in great detail in our December call.

The fourth quarter was the first step forward in really delivering on those operational commitments we laid out in that time horizon. CDIY and Industrial posted very strong revenue and growth, which we were pleased with.

And we're also very pleased with our Security recovery, as it really is underway. And we saw notable improvements in our North American business that John discussed. And all the actions are in place to drive the European business in a similar fashion over the next 12 to 18 months.

For 2014, we're very focused on improving our near-term returns and enhancing our operating leverage. And, as a result, our organic growth initiative is still a very significant part of our priorities. But we're really trying to leverage the investments that we've already made. We're not looking to make new investments in 2014 beyond those investments.

The Security margin improvement, 150 basis points, is a key priority, as well. We've taken surgical cost actions across our other businesses to ensure that operating leverage that I mentioned in the CDIY and Industrial segments. And then we'll never forget about the importance of staying focused on working capital, ensuring that we continue to show improvement year over year.

We are again focused on making sure that our capital allocation is a bit rebalanced for the next two years, as we will continue our acquisition moratorium, be focused on deleveraging our balance sheet, and repurchasing our shares of up to $1 billion over the next two years. This really positions our Company, we believe, to deliver on our long-term financial objectives.

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

Don, thanks. Lorraine, we can now open the call to Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Rich Kwas from Wells Fargo.

Rich Kwas - *Wells Fargo Securities - Analyst*

Hi, good morning, everyone. Two questions.

On the Security margin improvement, Don, can you give us a framework within the full-year guidance of what you expect European margin to be. It was 4% in the fourth quarter. At the low end of the range -- what do you need to get to the low end of the range in Europe and then what do you need to get to the high end?

And then for 2014, how much of a recovery in non-residential construction in the US are you assuming, and what's embedded in the guidance? Thanks.

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

Rich, good morning. European Security, as I mentioned, I think the first half we'll continue to see some challenges, although we expect some modest improvement in the operating margin rate in the first half of the year. But many of the cost actions, first of all, will not be implemented until June-July time frame, given the process of the European Union and the work councils that we discussed back in December.

However, we are very much focused on the revenue attrition side, RMR attrition, and making sure we slow that down in a significant way. So we expect to see improvement in that in the first half which will help the operating margins. So, I would say we'd see a modest improvement in the first portion of the year. And then the back half of the year is where we'd see a more significant component of improvement in that particular business.

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

Don, let me just -- because Rich will get cut off -- we're not going to forecast margins by business by quarter, Rich. You know that. But it's a very fair question, given the focus we've put on it. To help you in your modeling and in your thinking, at least for the year, we've said we're modeling and planning a 150 basis point increase in the our Security business.

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

In total.

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

The US is operating -- it always can improve but is operating at or near historical margins. And Europe is 40% of the business, of our Security business. You are more than capable of doing the math. And, as Don said, it will be more back-loaded than front-loaded because things take time in Europe. But, hopefully, that will help you without us getting into dicing and slicing businesses that we have no intention of doing.

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

Yes. And then on your second question, Rich, about non-resi and what we've put in our outlook for 2014, we really haven't factored a dramatic improvement in the non-resi industry within our guidance.

Most of our guidance is focused on general market performance today, as well as, in the case of Security in North America, very much focused on the vertical organic initiatives that John touched on, really trying to continue to enhance those, push those forward, and make more progress than we saw in 2013. Which the progress we saw in 2013 was very encouraging but our expectation is that's going to continue to really leverage the organic growth story within the North American business.

Operator

Peter Lisnic from Baird.

Josh Chan - *Robert W. Baird & Co. - Analyst*

Good morning. This is Josh Chan filling in for Pete. I was wondering about your North American margin performance this quarter. Do you consider that to be a long-term run rate? Or do you see further improvement in that level ahead? And if so, what will be the driver for further improvement, even from this level?

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

Don will take it. North America consists of three different businesses, so he'll have to take it piece by piece.

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

You're talking about North American Security specifically, I would assume?

Josh Chan - *Robert W. Baird & Co. - Analyst*

Security margins, yes.

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

That helps clarify. I think, as John mentioned, we are closely approaching historical levels for that. So, although we do expect it to get better slightly beyond what we saw in the fourth quarter in 2014, we did take some cost actions, as I mentioned, in this business that will help that performance. We are going to continue to move forward on the vertical organic growth initiatives, which are gross margin accretive to that business, and enhance the margin performance.

So, all those things that we're doing. And, of course, the SMS transition as we continue to work through that and leverage up that business as the volume improves, but also improve margins. So, we would expect it to improve. But you also have to recognize that it's at a high level but it's probably at the low end of the range of historical levels.

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

Let me just supplement that, to remind you. When Don talked about first-quarter guidance and fourth quarter, remember, first quarter for our Company has some seasonality. In CDIY, as everyone knows, January's a very soft month because that's when our large retail customers end their fiscal year and have a close eye, for very good reason, have a close eye on their inventory. So, in CDIY, it's about a two-and-a-half month quarter as opposed to a three-month quarter.

But, more importantly, Security historically, and this continues in North America, is a business with some seasonality. And historically if you looked, our second and third quarters from a margin perspective historically, all things being equal, are better than first and fourth. There's two reasons for that. Most of it's in the mechanical area.

But in the fourth and first quarters, particularly our Stanley access technologies business, to a lesser extent our mechanical locking business, we get into weather issues on install. We're scheduled to do a job, there's a snowstorm, the foundation isn't poured, we can't put in the door or we can't upgrade the door. Those are real issues that can have some headwind in the fourth and first quarter.

Secondly, our education vertical, for obvious reasons, performs much stronger in the second and third quarter. We do a lot more work in the education vertical in the months of a little bit of June, but particularly July and August when there are fewer students on campus and we're allowed to do that work. So, as you're looking at quarters and years, and doing your modeling -- and we're happy to talk about it because we've got a lot of history -- just do keep those two things in mind.

Operator

Jason Feldman from UBS.

Jason Feldman - *UBS - Analyst*

Good morning. On Security, I'm just curious what kind of visibility you have to flat or better Security sales next year, given the headwinds that you faced. And if you can also put the double-digit order growth in European Security into context for us. With mid-teens attrition, is mid double-digit order growth what you need to keep the business flat? Or is there some different way that we should be thinking about that?

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

Jim wants everybody to know he's alive and well and we hope you can hear him, Jason. I picked him up.

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

This is my 58th consecutive quarterly conference call and I didn't want to miss it. So, bear with me. I apologize for the voice.

But taking them separately, North America and Europe, in total, they'll be flat to slightly up. Europe will be slightly down for the year. With 10% attrition we need 5% order growth to be flat basically, because the RMR part of the portfolio is about 50% of the portfolio. So, we expect to go from where we are today, which is mid-teens attrition, down to about 10% attrition by the middle of the year. We will have about 12% attrition for the year. Which means we would need an order rate in excess of 6% to be positive.

We're not expecting to be positive in Europe on an organic basis in 2014 but we do expect that attrition to come down, and over time we'll convert that order backlog that we have into sales. And we're working very diligently on making sure that we have all the routines in place to make sure we do that effectively.

We have good momentum going in the verticals, as has been mentioned previously in North America. So that gives us a lot of confidence that we will have positive organic growth in North America. We see positive trend in Access Technologies, positive trend in CSS. The big question mark in SMS.

We have positive unit volumes for the first time in many years in mechanical. We think we're going to have a favorable market ahead of us. We've got a lot of work being done in specifying on construction jobs. And so all signs are positive but it's still a work in progress in the mechanical business in North America.

Operator

Sam Darkatsh from Raymond James.

Sam Darkatsh - *Raymond James & Associates - Analyst*

Good morning, John, Jim, Don. And, Jim, I hope you're feeling better.

Two questions. I'll ask them quickly in case I get cut off. The first one, last year you mentioned, John, that the first quarter represents about 18% to 19% historically of annual earnings. And your guidance here of $0.95 to $0.98 versus your annual guidance is still in that 18% to 19% range.

But I would think it would be lower than that this year because of the Security gains in margin as the year progresses, some of the restructuring savings as it progresses. So, why wouldn't the first quarter this year be lower as a percentage of the overall expected earnings? That would be question one.

The second question would be, based on the FX challenges in the emerging markets, are you contemplating paring back some of your discretionary spending in 2014 based on the macro and current currency headwinds there? Thank you.

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

Dan, it's Don. I'll take those questions.

The first one, the 18% to 19% was actually a 10-year historical range that we experienced, almost more before the merger. When you look at the post-merger Company, and we saw it again in 2013, the first quarter represents more of a 20% to 21% of the full year. And so that's really, in my view, the new starting base of this company, when you look at first quarter to total year. And that's why I think the 18% actually is down slightly from that range because of the items I mentioned of FX and tax that are driving that.

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

And the items that Sam mentioned.

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

And the items you mentioned, as well. And then as far as your other question around discretionary costs, yes, we are very much focused as a Company on dramatically controlling our discretionary costs. We obviously took a very significant restructuring program across the Company in the fourth quarter and have executed many of those actions. We still have many that we have to do, especially in Europe.

But, just as importantly, the costs, or the non-people costs, we are very much focused on reducing travel, where we have certain consulting activities we've cut way back on those levels of activities. The other costs related to anything that's connected to a person, phone cost, et cetera, we're very much focused on how we can reduce.

Some of it's contractual in nature. So we negotiate with our vendors. In others, it's just more of a policy change or a volume level of activity. That's something that will be one of our top five priorities for the year until we see more stabilization, especially in emerging markets.

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

Sam, I'll just add, because you won't get a follow-up, SG&A is something we talk about in great detail at the highest levels of this Company, and with our Board. And all SG&A, or discretionary cost if you want to use that term, as we've said many times, it isn't bad. Our investment in brands, our investment in people, in feet on the street, our investment in product development, building SBUs, is the last place where we're going to pare back.

What we may do is slow the pace of acceleration. There was a huge incremental lift in that in 2013. But we truly do, as I think most companies do in good conscience, divide all discretionary costs into two buckets, those that are creating revenue, generating new products, creating revenue and building brand franchises, versus those that are just required to run our business.

And it's the latter that's under closer scrutiny than ever and looking at significant cuts. The former will not increase at the rate they increased in 2013, nor were they ever planned to. They'll be closer to flat in 2014.

Operator

Mike Wood from Macquarie.

Mike Wood - *Macquarie Capital Partners - Analyst*

Hi. Thank you. On the update call you hosted last month you talked about 12% attrition. My understanding that may have been for November, but it seems like for the quarter it was back up in mid teens in your presentation. Can you just talk about how that is versus your expectations?

And to the extent the attrition is driven by any kind of irrational price competition, would you be chasing that business or would you just cede that share? Thank you.

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

Mike, I'll give you a top line -- this is John -- and then you can follow up with Greg because he can give you as much detail as you want that we feel we're willing to publicly disclose. What you said is correct. We were improving at a faster rate, quite frankly, than we expected in November. And it digressed or reverted in December, so the quarter ended up being flat sequentially in terms of attrition.

That being said, I don't manage this business, nor does Massimo Grassi who runs it day to day or even quarter to quarter. Obviously we look at the trends. Second half versus first half we were down 200 basis points. If we repeat that again in the first half, we'll be down 200 or 300 basis points.

And, as Jim said, our target by the end of the year is 10. We're tracking to get there or slightly short of it. That remains our objective.

But your statement is absolutely correct. December was poor relative to October, November, and we've not reduced the focus on it one bit.

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

The only thing I would add to that is that we really highlighted that in December as an encouraging sign. But in October, when we provided guidance, our expectation was that the attrition was going to be flat in the fourth quarter versus the third quarter, which is really what we saw. So we really highlighted that in December, more that we were seeing potential for encouragement there, and we still see that. But this business will see those types of fluctuations month to month.

Operator

Michael Dahl of Credit Suisse.

Michael Dahl - *Credit Suisse - Analyst*

Hi. Thanks. I wanted to ask about Security also, but on the North American side. Could you talk about what trends you're seeing on the RMR in North America, what type of conversion you're getting from some of the stronger install? And also maybe talk about which verticals you're seeing the most momentum in. Thanks.

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

I'll talk about which verticals we're seeing the most momentum in, which I already did in the presentation. With our global customers, with healthcare and in education. We're not going to talk about the beginning of your question. It's nothing we do in the public domain and that we think it would provide more, I'll say, competitive damage than it would be helpful information to our investor base. Jim may want to add something, too.

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

The way I would answer that question is that our RMR base without any acquisitions grew in 2013. So it is moving in the right direction. We're not going to talk about specific RMR attachment rates. And the verticals, did you want to mention anything else?

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

I did.

Operator

Ken Zener from KeyBanc.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Good morning. With 1Q guidance coming in below consensus, I just want you to be as clear as possible. The $60 million FX, is that going to be split equally 1Q and 2Q since it's front loaded, A? And, B, is your 1Q tax rate higher than your 21% to 22% guidance for the year? First question.

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

The $60 million of FX is pretty much divided in half, Q1, Q2. It's not perfect that way but that's a good way to think about it. And the tax rate for Q1 this year will be relatively in line with our expectation for the full year. But remember that in the first quarter of last year the tax rate was around 16%.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Correct. Thank you.

And then if you could give us lessons learned as well as educate us on emerging market, since you're accessing more selling points there. Part of the decelerated expectation in growth I think was related to probably lower demand, A. But it was also some excess load-in that you guys might have perceived as demand.

So, how do you guys manage those channels of distribution given that they're less technical, you have less weekly runs of data in terms of sell-through and sell-in. What did you learn in 2013? And how are those channels different than the big box we're used to domestically? Thank you.

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

If you're talking about load-in issues, we did mention last quarter that there was some issues, in particular in China, with respect to the distribution channels becoming congested as we grew our T2 distribution channel in China. What we're really finding in China, as we sit here today, is there a deceleration going on in the market. And there is a credit crunch going on. And we're starting to really see a very tight credit situation with the channel.

So it's not as much of a load-in issue as an ability of the distributors to finance purchases to meet what could be growing end-user demand. But with the issue in the channel it's almost impossible for the distributors to buy the product that they need.

And it's a really interesting phenomenon going on in China right now. If you've been following the news over the last couple days, there's been some indication from the central bank in China that they are beginning to realize that there's a credit crunch with the small- to mid-sized businesses and we're seeing that.

Operator

David MacGregor from Longbow Research.

David MacGregor - *Longbow Research - Analyst*

Yes, good morning everyone. I was hoping you can go back and just talk a little more about the attrition rates and some of the market dynamics around those attrition rates. And specifically, is this a dissatisfaction with historical Niscayah execution or is it a reaction to increased effort by your competitors?

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

It's some of each, David, as we've discussed on previous calls. We've had a lot more price discipline, the Niscayah European model. And Jim's gone into great detail on this on previous calls. And Greg, I know, will be happy to provide or reinforce that offline. In the interest of time I'll try to do it quickly.

We're trying to turn this organization from farmers to hunters. Historically Niscayah relied on referrals from its parent company, Securitas. And those have gone away.

It was much more of an install model with less attachment than the model that Stanley Convergent Security Solutions, both in US and Europe, have operated. So there was essentially a model change, or the way business was done change, as a result of our acquisition of Niscayah. And, quite frankly, we or they, the Niscayah folks, relied more on those referrals than we realized. Thus, attrition was higher.

Second has been pricing discipline on our part. If in fact we're going to do an installation, we've gotten much better at costing. We want to be sure those are at least, at worst, breakeven, if it has some RMR attached to it, otherwise that it's at a reasonable margin. That also has contributed to the growing attrition.

And, thirdly, is we've changed a lot of people. The folks that we're relying on the referrals, and it's not even meant to be derogatory, but were much more farmers than hunters, weren't going to make it in the system and business that we're trying to operate. And we believe we have very capable leaders.

But in four of our largest markets we have new general managers in those markets in place within the last six months. They've come either from the industry or related industries, from blue chip companies, all of whom Jim, Don, myself have met, and Brett and Massimo have interviewed intensively. So, we think we've got a new team on the field that's going to help, as well. So you've got a lot of factors contributing to it. You touched on a couple. And hopefully I added a little more light. But please follow up with Greg and Dennis and they'll --.

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

I would just add, there's one other competitive dynamic which is relevant here, which is that the electronics are gradually, and maybe now at an accelerating rate replacing cards in commercial buildings and establishments. This places tremendous pressure on the guarding companies. That's one reason I suspect that Securitas probably tried to acquire Niscayah, because of its electronic capabilities.

Without an electronic company, you have several major European security companies which are guard-focused and fairly large. And their typical operating margin appetite is about a 4% to 6% operating margin. That's quite satisfactory to them.

So that competition for what I'll call the commodity-type services is pretty intense right now in Europe, and probably more intense than it has been in years. For us, the answer is moving to the vertical solutions that we're implementing in North America. But in order to do that, first we have to get the sales force in place, which we've done, and we're working on maturing that sales force now.

We're working on getting the attrition down to stabilize the revenue base, mature the organization enough so it can handle the vertical market solutions. And that's about 6 to 12 months out.

Once we start getting the vertical market solutions from North America imported into Europe, that competitive pressure that we're feeling will be muted to some extent and the higher margin business that we'll bring in, and will really help turn the Niscayah situation around.

Operator

Michael Rehaut from JPMorgan.

Michael Rehaut - *JPMorgan Chase & Co. - Analyst*

Thanks. Good morning, everyone. A couple questions here, just don't want to get cut off.

Looking at, for a change of pace here, Construction and Industrial, if I calculate it right, stripping out the negative impact of FX, if you're saying that roughly 80% of the $60 million headwind was in CDIY, it looks like 2013 CDIY was about 15.7% margin. And it translates to a 33% incremental margin. Are those numbers right?

And as you think about that business going forward, do you look at a 30%, 35% incremental as a sustainable basis given that that business, I would say best case is a mid-teens to high-teens type margin business? Or how to think about that longer term.

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

I think if you -- the way you did the math around the currency to get to what's the operating margin rate without the currency is reasonably accurate. So I would agree with that. But you also have to remember that you're not seeing as much leverage in 2013 because we've made some growth investments, too, in SG&A, especially in emerging markets within CDIY.

I do think when the business stabilizes and we're not making those types of investments, which will be in the latter half of 2014 assuming no other changes in currency, that the leverage drop-through rate is more of a 35%, 38% number in that business versus what you're seeing now, because of both the FX and the growth investments.

Operator

Stephen Kim from Barclays.

Stephen Kim - *Barclays Capital - Analyst*

Thanks very much, guys. Just to follow up on that one, if you could explain what you think the incremental margins are in the other businesses, given the changes that have occurred.

And, more broadly, also, if you could talk about in CDIY and Industrial, you had some pretty good organic growth generally. I was curious how much of that you think is attributable to the initiatives that you've been doing in those businesses, implementing, versus, let's say, the overall market improvement.

Thanks.

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

As far as incremental margins, I mentioned CDIY already. Industrial has a very similar, depending of on the business, because there's four different businesses in there, can range anywhere from 30% to 35% incremental margins. Security is a different animal because it depends on the region, the type of business.

And it can have a different level of leverage or operating leverage depending on which piece of it. It can range anywhere from a 20% number to a 35% number. So that's difficult to really say that you have a perfect one for that.

I think the more important thing about Security right now is continuing its recovery, getting it to the levels of profitability that we want to see. At the same time, seeing the right levels of organic growth that are consistent with our long-term financial objectives. And then at that point, when that is stabilized, we can start to talk about what's the right level of leverage we're going to see in that business going forward.

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

Do you want to take the second part, Don -- how much of it was our initiatives. We said 200 basis points.

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

Security specifically?

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

No, I think Steve was asking about the whole portfolio. He won't get back on. Steve, what we said is roughly 200 basis points of our top-line growth we felt was attributable to the growth initiatives. To the extent we can maintain that growth rate at lower initiatives, obviously that will have a positive impact on incremental margin. If I got the gist of your question.

Operator

Liam Burke from Janney Capital Markets.

Liam Burke - *Janney Capital Markets - Analyst*

Yes, thank you. Good morning. John, you had another pretty decent contribution on the IAR side from Mac Tools. Is that market share gains or just firming end markets? And in Europe, you had promotional activity driving positive growth on the IAR side. Is that sustainable as the promotional activities ease off?

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

The promotional growth was more CDIY than IAR, Liam.

Liam Burke - *Janney Capital Markets - Analyst*

I'm sorry.

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

No worries. It is sustainable. We had terrific performance in IAR in Europe and CDIY in Europe. But I may have misspoken or you misunderstood. There was much promotion -- I shouldn't say that -- it's a busy promotional quarter for CDIY in Europe in the fourth quarter because of the strength of the Black & Decker consumer products franchise, in Europe in general and in the UK in particular.

That being said, I did talk about Equip'Auto which normally happens -- often happens in September. This year it just happened to happen in October. From a US perspective, think Mac Tools Fair. It's a huge Pan-European exhibition that does contribute positively to revenue, and it was very well-received. So I might have sent you a mixed signal there.

In terms of Mac, it's going from -- you've followed us a long time, and Jim has been reporting on this longer. I'm just going to help him save his voice. It's gone from bad to good, and it's going from good to better. And it's a combination of several things.

We've really worked hard on net distributor adds. We've worked really hard on having the right distributors and their productivity -- mentoring, training, retaining. But it's also what they have on their truck. We have an improved financing program for them, which is far more competitive than what we've sent them to battle with in the past. Our Treasury Department deserves a lot of credit for that.

That's the underlying points. But, in fact, what they've got on their trucks is a lot better than what they've had before. It was overwhelmingly 100% sourced business with no proprietary technology. Now a significant percentage of what they're selling are produced in our facilities ever since we combined Mac, Proto and Vidmar under one leadership team, made it part of North American IAR. Those cross-SBU synergies are really gaining traction. We also have the capability since the merger to have DeWalt tools on a Mac dual truck. That's a big draw.

So, we've got a lot of things in terms of basic blocking and tackling that we've improved with Mac. But I think, most importantly, we've got a dramatically better line of products on the truck in terms of both what we're offering, innovation, margin for the distributor. And it's all working to make this -- it's always been a good franchise. Now it's a good business and it's going to do nothing but become a better business under the leadership of the current management team.

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

And in the fourth quarter they celebrated their 16th consecutive quarter of organic growth. Which, for those of you that have been following the Company a long time, would find that almost miraculous.

Operator

Jeremie Capron from CLSA.

Jeremie Capron - *CLSA - Analyst*

Good morning. Could you comment on price-cost dynamics in your tools business, particularly CDIY, where you seem to be gaining share?

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

I would say that -- I said it before about our CDIY business. It's a situation that there is a fine balance of going after volume and controlling your pricing decisions in this business. I think there's many pieces of it that have significant levels of competition, especially on the power tool side, that you have to be smart about when you do promotional activities, how you do promotional activities. And ultimately the driver of many of those decisions is all the new product introductions that we put into the marketplace.

And ultimately those things drive the market share gains that we've experienced, especially the last several years. We made great progress, especially with our cordless power tool products, over that time horizon. And as a result we've been able to really continue to combat some of the price pressures you see in that particular space. But we all know that's a challenging aspect of this business. But as long as you have that DNA around new product introductions and driving technology and innovation into that marketplace that the user wants versus giving them something that they don't want, you ultimately can really continue to combat that.

I think you saw that in the performance where there's a modest price negative in the business in 2013. We're never satisfied with that. As we go into 2014 we want to continue to focus on how do we minimize that impact and maybe eventually turn that into a price positive.

But ultimately that's the dynamic of the business today. We're not satisfied with it but we think we have all the right, as I mentioned, DNA in the business that allows us to be very competitive, continue to have a premium to many of our competitors, as well.

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

Jeremy, let me just add on to that. We've said this before on calls. It's our largest business. We think it's well managed. And it has the benefit of being a market leader or number one or two in virtually every category where it competes. So it's not only our right, it's our obligation to behave like price leaders.

That being said, there's tremendous competition in the market, particularly in power tools. Which is relatively new to the Stanley management team post Black & Decker merger. Having said all that, operating margins were up 10 basis points, all-in. And the reason we've been able to do that and maintain it is real prices in this category, real prices, have declined 1% to 2% a year for the last 10 years.

We haven't mentioned productivity, operational excellence, whatever you'd like to call it on this call, but we work very hard at it. And our global operations team and our CDIY office team every year has an absolute table stakes commitment of 3% cost reduction. They usually have a funnel that adds to more than that. But if real prices go down 1% to 2% and margins are 35%, and you get a 3% cost reduction, that leads to margin maintenance. And that's how we manage this business.

So, quarter to quarter, we'll have a little more promotional activity that might drive a little more volume at a little lower margin. And that will be a little bit of give and take. But over time, that's how we think about this business. We want to keep it right in that mid-teens level and continue to gain share. And so far I think the CDIY team in every function's done a commendable job of doing that. And it is a model for the rest of our Company in terms of the level we're trying to get to.

Operator

Dennis McGill from Zelman & Associates.

Dennis McGill - *Zelman & Associates - Analyst*

Good morning. Thanks. Don, I was hoping you could just walk through a little bit on the math of how you think about the cash flows over the next couple of years. I think what you guided to is roughly $1 billion of share repos and then $700 million of debt reduction. That would seem to pretty much match the free cash flow that you'll generate. But then you have dividends of $600 million or $700 million, and then you've got some limitation on the international cash and how you use that. So, I was just wondering if you could maybe bridge all of that.

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

Yes. We went into the year with a debt level of about $300 million that we can actually pay down in commercial paper. And so that's about as much deleveraging as we can do going forward over the next couple years. So, that's the number for debt deleveraging. And then there's obviously the dividend numbers you mentioned and then share repurchase, as well. That pretty much uses up the vast majority of our cash flow over the next two years.

Dennis McGill - *Zelman & Associates - Analyst*

Is that inclusive of pulling back international cash?

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

There will be a little bit of that as well, absolutely.

Operator

And I will now turn the call back over to Mr. Greg Waybright for closing remarks.

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

Lorraine, thank you. We'd like to thank everyone again for calling in this morning and for your participation. And please contact me if you have any further questions. Thank you.

Operator

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