

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K
ANNUAL REPORT

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934 [FEE REQUIRED]

For the fiscal year ended January 3, 1998

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 [NO FEE REQUIRED]

For the transition period from to

COMMISSION FILE 1-5224

THE STANLEY WORKS
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

CONNECTICUT 06-0548860
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER
INCORPORATION OR ORGANIZATION) IDENTIFICATION NUMBER)

1000 STANLEY DRIVE
NEW BRITAIN, CONNECTICUT 06053
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

(860) 225-5111
(REGISTRANT'S TELEPHONE NUMBER)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

| TITLE OF EACH CLASS | NAME OF EACH EXCHANGE ON WHICH REGISTERED |
|--|--|
| Common Stock--Par Value \$2.50 Per Share | New York Stock Exchange Pacific Exchange |

9% Notes due 1998*
7 3/8% Notes Due December 15, 2002
*repaid February 1, 1998

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark whether the registrant (1) has filed all reports
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of
1934 during the preceding 12 months and (2) has been subject to such filing
requirements for the past 90 days.

Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item
405 of Regulation S-K is not contained herein, and will not be contained, to
the best of registrant's knowledge, in definitive proxy or information
statements incorporated by reference in Part III of this Form 10-K or any
amendment to this Form 10-K [].

The aggregate market value of Common Stock, par value \$2.50 per share, held
by non-affiliates (based upon the closing sale price on the New York Stock
Exchange) on March 30, 1998 was approximately \$4.8 billion. As of March 30,
1998, there were 89,109,513 shares of Common Stock, par value \$2.50 per share,
outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Annual Report to Shareholders for the year ended January 3, 1998 are incorporated by reference into Parts I and II.

Portions of the definitive Proxy Statement dated March 9, 1998, filed with the Commission pursuant to Regulation 14A, are incorporated by reference into Part III.

Part I

Item 1. Business

1(a) Introduction. (i) General. The Stanley Works ("Stanley" or the "Company") was founded in 1843 by Frederick T. Stanley and incorporated in 1852. Stanley is a worldwide producer of tools, hardware and door products for professional, industrial and consumer use. Stanley(R) is a brand recognized around the world for quality and value.

In 1997, Stanley had net sales of \$2.7 billion and employed approximately 18,000 people worldwide. The Company's principal executive office is located at 1000 Stanley Drive, New Britain, Connecticut 06053 and its telephone number is (860) 225-5111.

(ii) July 1997 Restructuring Initiative. On July 18, 1997 the company announced a major initiative to reallocate resources in order to deliver profitable growth on a sustained basis. This growth will be fueled by increased spending on new product development, new ventures to expand the Company's markets and brand development with the savings achieved from streamlining operations and reorganizing into a product management structure. The company has moved from a portfolio company with 11 fully independent businesses to a single operating company comprised of eight product groups, three geographic regions and corporate leaders of brand development, operations, technology and several support functions. The support functions such as finance, human resources and information technology are being centralized. Manufacturing and distribution operations are being rationalized. The company plans to move from 83 manufacturing plants to 45 and from 40 distribution facilities to 25. The sales organization has been reorganized to reduce redundant coverage of key customers and channels. Overall, these actions will change the composition of the company's workforce and are expected to reduce net employment levels by 4,500 people.

1(b) Industry Segment Information. Financial information regarding the Company's industry segments is incorporated herein by reference from page 29 of the Company's Annual Report to Shareholders for the year ended January 3, 1998.

1(c) Narrative Description of Business. The Company's operations are classified into three industry segments: Tools, Hardware and Specialty Hardware.

Tools. The Tools segment manufactures and markets consumer, industrial and engineered tools. Consumer tools includes hand tools such as measuring instruments, planes, hammers, knives and

blades, wrenches, sockets, screwdrivers, saws, chisels, boring tools, masonry, tile and drywall tools, paint preparation and paint application tools. Industrial tools includes industrial and mechanics hand tools, including STANLEY-PROTO(R) industrial tools and MAC(R) mechanics tools, and high-density industrial storage and retrieval systems. Engineered tools includes STANLEY-BOSTITCH(R) fastening tools and fasteners used for commercial, industrial, construction, packaging and consumer use; hydraulic tools (these are hand-held hydraulic tools used by contractors, utilities, railroads and public works as well as mounted demolition hammers and compactors designed to work on skid steer loaders, mini-excavators, backhoes and large excavators); and air tools (these are high performance, precision assembly tools, controllers and systems for tightening threaded fasteners used chiefly by vehicle manufacturers).

Hardware. The hardware segment manufactures and markets hardware products ranging from hinges, hasps, shelf brackets, bolts and latches to a line of closet organizing systems and mirrored closet doors, door hardware and wall mirrors.

Specialty Hardware. The specialty hardware segment manufactures and markets residential insulated steel and reinforced fiberglass entrance door systems and automatic doors.

Competition. The Company competes on the basis of its reputation for product quality, its well-known brands, its commitment to customer service and strong customer relationships, the breadth of its product lines and its emphasis on product innovation. The Company is also striving to find new customers both within the markets that it currently serves and in new markets around the world.

The Company encounters active competition in all of its businesses from both larger and smaller companies that offer the same or similar products and services or that produce different products appropriate for the same uses. In 1997, the Company invested approximately \$84 million in facilities, new equipment, technology and software in order to achieve enhanced customer service, operational excellence in manufacturing and new product innovation.

In the Company's consumer hand tool and consumer hardware businesses, a small number of competitors produce a range of products somewhat comparable to the Company's, but the majority of its competitors compete only with respect to one or more individual products within a particular line. The Company believes that it is the largest manufacturer of consumer hand tools in the world and that it offers the broadest line of such products. The Company believes that its market position in the U.S. and Canada for consumer hardware is comparable to or greater than that of its major competitors and that it offers the

broadest line of hinges and home hardware, which represents the most important part of its hardware product sales.

In the Company's industrial tool business in the U.S., the Company believes that it is the leading manufacturer of high-density industrial storage cabinets. In the Company's engineered tool business in the U.S., the Company believes that it is the leader in the manufacture and sale of pneumatic fastening tools and related fasteners to professional contractors and to the furniture and pallet industries as well as the leading manufacturer of hand-held hydraulic tools and a leading manufacturer of mounted hydraulic tools. In 1997, there was significant price erosion for certain fastening tools manufactured by the Company. Highly engineered fastening tools have historically been protected from low-cost foreign sourced competition due to a market preference for a higher quality U.S. made product. The introduction of foreign sourced tools of an acceptable quality resulted in significant pricing pressure on the market for these products. In addition, the Company reduced its prices in Europe in a strategic response to market conditions.

In the Company's hardware business in the U.S., the Company believes that it is a leading manufacturer of builders and architectural hardware products, mirrored closet doors and hardware for sliding, folding and pocket doors and the leading supplier of wall mirrors.

In the Company's specialty hardware business, the Company believes that it is the leader in the U.S. with respect to the manufacture and sale of insulated steel residential entrance doors as well as the leader in the U.S. in the manufacture, sale and installation of power-operated sliding doors.

Customers. A substantial portion of the Company's products are sold through home centers and mass merchant distribution channels in the U.S. In 1997, approximately 12% of the Company's consolidated sales were to The Home Depot. A consolidation of retailers in the home center and mass merchant distribution channel is occurring. These customers constitute a growing percent of the Company's sales and are important to the Company's operating results. While this consolidation and the domestic and international expansion of these large retailers provide the Company with opportunities for growth, the increasing size and importance of individual customers creates a certain degree of exposure to potential volume loss. The loss of Home Depot as well as certain of the other larger home centers as customers would have a material adverse effect on each of the Company's business segments until either such customers are replaced or the Company makes the necessary adjustments to compensate for the loss of business.

Raw Materials. The Company's products are manufactured primarily of steel and other metals, although some are of wood or plastic. The raw materials required are available from a number of sources at competitive prices and the Company has relationships of long standing with many of its suppliers. The Company has experienced no difficulties in obtaining supplies in recent periods.

Backlog. At February 7, 1998, the Company had \$135 million in unfilled orders compared with approximately \$149 million in unfilled orders at February 1, 1997. All these orders are reasonably expected to be filled within the current fiscal year. Most customers place orders for immediate shipment and as a result, the Company produces primarily for inventory, rather than to fill specific orders. The Company has begun implementation of demand flow production, which aligns inventory levels with actual demand, in three of its manufacturing facilities.

Patents and Trademarks. No business segment is dependent, to any significant degree, on patents, licenses, franchises or concessions and the loss of these patents, licenses, franchises or concessions would not have a material adverse effect on any business segment. The Company owns numerous patents, none of which are material to the Company's operations as a whole. These patents expire from time to time over the next 17 years. The Company holds licenses, franchises and concessions, none of which individually or in the aggregate is material to the Company's operations as a whole. These licenses, franchises and concessions vary in duration from one to 17 years.

The Company has numerous trademarks that are utilized in its businesses worldwide. The STANLEY(R) and STANLEY (in a notched rectangle)(R) trademarks are material to all three business segments. These well-known trademarks enjoy a reputation for quality and value and are among the world's most trusted brand names. In addition, in the Tools segment, the Bostitch(R), Powerlock(R), Tape Rule Case Design (Powerlock)(R), LaBounty(R), MAC Tools(R), Proto(R), Jensen(R), Goldblatt(R) and Vidmar(R) trademarks are material to the business.

Environmental Regulations. The Company is subject to various environmental laws and regulations in the U.S. and foreign countries where it has operations. Future laws and regulations are expected to be increasingly stringent and will likely increase the Company's expenditures related to environmental matters.

The Company is involved with remedial and other environmental compliance activities at some of its current and former sites. Additionally, the Company, together with many other parties, has been named as a potentially responsible party ("PRP") in a number of administrative proceedings for the

remediation of various waste sites, including nine Superfund sites. Current laws potentially impose joint and several liability upon each PRP. In assessing its potential liability at these sites, the Company has considered the following: the solvency of the other PRP's, whether responsibility is being disputed, the terms of existing agreements, experience at similar sites, and the fact that its volumetric contribution at these sites is relatively small.

The Company's policy is to accrue environmental investigatory and remediation costs for identified sites when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The amount of liability recorded is based on an evaluation of currently available facts with respect to each individual site and includes such factors as existing technology, presently enacted laws and regulations, and prior experience in remediation of contaminated sites. The liabilities recorded do not take into account any claims for recoveries from insurance or third parties. As assessments and remediation progress at individual sites, the amounts recorded are reviewed periodically and adjusted to reflect additional technical and legal information that becomes available. As of January 3, 1998, the Company had reserves of \$32 million, primarily for remediation activities associated with company-owned properties as well as for Superfund sites.

The amount recorded for identified contingent liabilities is based on estimates. Amounts recorded are reviewed periodically and adjusted to reflect additional technical and legal information that becomes available. Actual costs to be incurred in future periods may vary from the estimates, given the inherent uncertainties in evaluating environmental exposures. Subject to the imprecision in estimating future environmental costs, the Company does not expect that any sum it may have to pay in connection with environmental matters in excess of the amounts recorded will have a materially adverse effect on its financial position, results of operations or liquidity.

Power-generating Subsidiary. Under the General Statutes of Connecticut, the Company is deemed to be a "holding company" that controls an electric company as a result of its being the sole shareholder of Farmington River Power Co., a power-generating subsidiary of the Company since 1916. Under such statute, no organization or person may take any action to acquire control of such a holding company without the prior approval of the Connecticut Department of Public Utility Control.

Employees. During 1997, the Company had approximately 18,000 employees, approximately 12,000 of whom were employed in the U.S. Of these U.S. employees, approximately 20% are covered by collective bargaining agreements with approximately 9 labor unions. The majority of the Company's hourly- and weekly-paid

employees outside the U.S. are covered by collective bargaining agreements. The Company's labor agreements in the U.S. expire in 1998, 1999, 2000 and 2001. There have been no significant interruptions or curtailments of the Company's operations in recent years due to labor disputes. The Company believes that its relationship with its employees is good.

Cautionary Statements. Certain risks and uncertainties are inherent in the Company's ability to achieve operational excellence and deliver sustained, profitable growth to its shareholders.

The Company's drive for operational excellence is focused on improving customer service, consolidating multiple manufacturing and distribution facilities, outsourcing non-core activities and converting to common systems. The ability to implement the initiatives associated with these goals is dependent on the Company's ability to manufacture products that meet customer requirements for on-time delivery, quality and value and the ability to develop and execute comprehensive plans for the facility consolidations; the ability of the organization to complete the transition to a product management structure without losing focus on the business; the availability of vendors to perform the non-core functions; the successful recruitment and training of new employees; the resolution of any labor issues related to closing facilities; the need to respond to significant changes in product demand during the transition; and unforeseen events.

The Company's ability to generate sustained, profitable growth is dependent on successfully freeing up resources to fund new product and brand development and new ventures to broaden its markets and to defend market share in the face of intense price competition. Success at developing new products will depend on the ability of the new product development process to foster creativity and identify viable new product ideas as well as the Company's ability to attract new product engineers. The achievement of growth through new ventures will depend upon the ability to successfully identify, negotiate, consummate and integrate into operations acquisitions, joint ventures and /or strategic alliances.

The Company's ability to achieve and sustain the improvements resulting from these initiatives will be dependent on the extent of pricing pressure within the Company's markets and other changes in its competitive markets, the continued consolidation of customers in consumer channels, increasing global competition, changes in trade, monetary and fiscal policies and laws, inflation, currency exchange fluctuations, the impact of currency exchange rates on the competitiveness of the Company's products and recessionary or expansive trends in the economies in which the Company operates.

1(d) Financial information about foreign and domestic operations and export sales. Geographic area information on page 29 of the Annual Report to Shareholders for the year ended January 3, 1998 is incorporated herein by reference.

Item 2. Properties.

As of January 3, 1998, Registrant and its subsidiaries owned or leased facilities for manufacturing, distribution and sales offices in 31 states and 30 foreign countries. The Registrant believes that its facilities are suitable and adequate for its business.

A summary of material locations (over 50,000 square feet) that are owned by the Registrant and its subsidiaries are:

Tools

Phoenix, Arizona; Visalia, California; Clinton and New Britain, Connecticut; Shelbyville, Indiana; Kansas City, Kansas; Two Harbors, Minnesota; Hamlet, North Carolina; Columbus, Georgetown and Sabina, Ohio; Allentown, Royersford and York, Pennsylvania; East Greenwich, Rhode Island; Cheraw, South Carolina; Shelbyville, Tennessee; Dallas and Wichita Falls, Texas; Pittsfield and Shaftsbury, Vermont; Heidelberg West and Ingleburn, Australia; Smiths Falls, Canada; Pecky, Czech Republic; Ecclesfield, Hellaby, Manchester and Sheffield, England; Besancon Cedex and Maxonchamp, France; Wieseth, Germany; Chihuahua and Puebla, Mexico; Wroclaw, Poland; Taichung Hsien, Taiwan; and Amphur Bangpakong, Thailand.

Hardware

Chatsworth and San Dimas, California; New Britain, Connecticut; Richmond, Virginia; Brampton, Canada; Sheffield, England; and Marquette, France.

Specialty Hardware

Farmington, Connecticut and Troy, Michigan.

A summary of material locations (over 50,000 square feet) that are leased by the Registrant and its subsidiaries are:

Tools

Costa Mesa, California; Covington, Georgia; Fernley, Nevada; Charlotte and Kannapolis, North Carolina; Cleveland and Columbus, Ohio; Milwaukie, Oregon; Carrollton, Texas; Burlington, Canada; and Northampton, England.

Hardware

Tupelo, Mississippi; and Oakville, Ontario.

Specialty Hardware

Orlando, Florida; Winchester, Virginia; Langley and Montreal, Canada.

Item 3. Legal Proceedings.

On November 30, 1995, the U.S. Department of Justice ("DOJ") filed a civil complaint against the Company and sixteen other defendants pursuant to the Federal Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"). Under CERCLA, the DOJ can seek to impose strict liability and joint and several liability on liable parties.

The DOJ is seeking recovery of past response costs of approximately \$1.3 million incurred by the United States Environmental Protection Agency ("EPA") at the Erie Coatings and Chemicals ("Erie") site in Erie, Michigan and a declaratory judgment that the defendants are liable for future response costs. The majority of the EPA's response costs were incurred in removing drums of materials from the site. The EPA also conducted some limited soil removal. It is the Company's understanding that it is unlikely that any additional significant remediation work will be necessary.

On October 24, 1996, a group of eight defendants, including the Company (the "settling defendants") filed a third party contribution claim against 23 parties and a counterclaim against various federal agencies that sent materials to the site. On April 4, 1997, the settling defendants along with eleven third-party defendants reached a settlement with the government for \$900,000 to resolve their respective liabilities for past response costs. The Company agreed to pay \$112,801. The court entered the consent order regarding the settlement on August 11, 1997. The settlement does not resolve the government's potential claims against the settling parties for response costs that are incurred after the settlement date. However, the Company believes that it is unlikely that any additional significant remediation work will be necessary. If this is not the case, the government likely will bring claims against the settling defendants, including the Company, to recover such costs.

In the normal course of business, the Company is involved in various lawsuits and claims, including product liability and distributor claims. The Company does not expect that the resolution of these matters will have a materially adverse effect on the Company's consolidated financial position, results of operations or liquidity.

Item 4. Submission of Matters to a Vote of Security Holders.

No matter was submitted during the fourth quarter of the Registrant's last fiscal year to a vote of security holders.

Executive Officers. The following is a list of the executive officers of the Registrant as of January 3, 1998:

| Name, Age, Birth date | Office | Elected to Office |
|---------------------------------------|--|-------------------|
| J.M. Trani (53) (3/15/45) | Chairman and Chief Executive Officer. Joined Stanley December 31, 1996; 1986 President and Chief Executive Officer of GE Medical Systems. | 12/31/96 |
| J.A. Cosentino, Jr.(48) (11/12/49) | Vice President, Operations. Joined Stanley October 1997; 1997 President/CEO Todd Combustion, Inc.; 1995 CEO, Rau Fastener Company, L.L.C.; 1990 President, Otis Elevator Company - N.A. Operations. | 10/29/97 |
| W.D. Hill (48) (9/18/49) | Vice President, Engineering. Joined Stanley August 1997; 1996 Director Product Management - Tool Group, Danaher Tool; 1994 Vice President, Product Development Global Accessories, The Black & Decker Corporation; 1992 Vice President Product Development - N.A. Power Tools, The Black & Decker Corporation. | 9/17/97 |
| K.O. Lewis (44) (5/28/53) | Vice President, Marketing and Brand Management. Joined Stanley November 1997; 1996 Executive Vice President Strategic Alliances, Marvel Entertainment Group; 1986 Director Participant Marketing, Walt Disney Attractions. | 11/3/97 |
| T.E. Mahoney (56) (3/20/42) | President, Consumer Sales Americas. Joined Stanley in 1965; 1995 Vice President, Marketing Development and President and General Manager of Stanley Customer Support Division; 1992 President and General Manager, Stanley Hardware. | 6/5/95 |

| | | |
|--------------------------------|--|---------|
| M.J. Mathieu (46) (2/20/52) | Vice President, Human Resources. Joined Stanley September 1997; 1996 Manager - Human Resources, GE Motors & Industrial Systems (Fort Wayne, Indiana); 1994 Consultant - Executive Staffing, General Electric Company (Fairfield, Connecticut); 1989 Consultant - Union Relations, General Electric Company. | 9/17/97 |
| P.W. Russo (44) (5/23/53) | Vice President, Strategy and Development. Joined Stanley in 1995; 1991 Co-Chairman and Co-Chief Executive Officer, SV Corp. (formerly Smith Valve Corp.); 1988 Co-founder and Managing Director, Cornerstone Partners Limited. | 9/18/95 |
| J.E. Turpin (51) (6/9/46) | Vice President, Operational Excellence. Joined Stanley in 1970; 1995 Vice President Operations, The Stanley Works; 1992 President & General Manager, Stanley Air Tools. | 4/23/97 |
| S.S. Weddle (59) (11/9/38) | Vice President, General Counsel and Secretary. Joined Stanley in 1978. | 1/1/88 |
| T.F. Yerkes (42) (9/9/55) | Vice President and Controller. Joined Stanley in 1989; 1990 Director of Accounting and Financial Reporting. | 7/1/93 |

Executive officers serve at the pleasure of the Board of Directors. Unless otherwise indicated, each officer has had the same position with the Registrant for five years.

Part II

Item 5. Market for the Registrant's Common Stock and Related Stockholder Matters. Registrant incorporates by reference the line item "Shareholders of record at end of year" from pages 22 and 23 and the material captioned "Investor and Shareowner Information" on page 45 of its Annual Report to Shareholders for the year ended January 3, 1998.

Item 6. Selected Financial Data. Registrant

incorporates by reference pages 22 and 23 of its Annual Report to Shareholders for the year ended January 3, 1998.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations. Registrant incorporates by reference pages 24 through 28 of its Annual Report to Shareholders for the year ended January 3, 1998.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk. Registrant incorporates by reference the material captioned "Market Risk" on page 27 of its Annual Report to Shareholders for the year ended January 3, 1998.

Item 8. Financial Statements and Supplementary Data. The consolidated financial statements and report of independent auditors included on pages 30 to 43 and page 21, respectively, of the Annual Report to Shareholders for the year ended January 3, 1998 are incorporated herein by reference.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure. None.

Part III

Item 10. Directors and Executive Officers of the Registrant. Information regarding the Company's Executive Officers appears in the "Executive Officers" section at the end of Part I of this report. In addition, the Registrant incorporates by reference pages 1 through 4 of its definitive Proxy Statement, dated March 9, 1998.

Item 11. Executive Compensation. Registrant incorporates by reference the last paragraph of "Information Concerning Directors Continuing in Office" on page 4 and the material captioned "Executive Compensation" on pages 6 through 14 of its definitive Proxy Statement, dated March 9, 1998.

Item 12. Security Ownership of Certain Beneficial Owners and Management. Registrant incorporates by reference the material captioned "Security Ownership" on pages 5 and 6 of its definitive Proxy Statement, dated March 9, 1998.

Item 13. Certain Relationships and Related Transactions. None.

Part IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K.

14(a) Index to documents filed as part of this report:

1. and 2. Financial Statements and Financial Statement Schedules.

The response to this portion of Item 14 is submitted as a separate section of this report (see page F-1).

3. Exhibits

See Exhibit Index on page E-1.

14(b) The following reports on Form 8-K were filed during the last quarter of the period covered by this report:

| Date of Report ----- | Items Reported ----- |
|-------------------------|---|
| October 15, 1997 | Press releases, dated October 15, 1997 announcing hiring of new Vice President, Marketing and Brand Development and third quarter results. |
| October 29, 1997 | Press release dated October 29, 1997 announcing the hiring of a Vice President, Operations. |
| November 10, 1997 | Press release dated November 10, 1997 announcing the acquisition of Atro Industriale S.p.A. |
| December 15, 1997 | Announcement that R. Alan Hunter, President and Chief Operating Officer was leaving the company and designation of "executive officers" and "officers" as of January 1, 1998. |

14(c) See Exhibit Index on page E-1.

14(d) The response to this portion of Item 14 is submitted as a separate section of this report (see page F-1).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE STANLEY WORKS

By John M. Trani

John M. Trani, Chairman
and Chief Executive Officer

February 25, 1998

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on February 25, 1998 by the following persons on behalf of the Registrant and in the capacities indicated.

John M. Trani

James G. Kaiser

John M. Trani, Chairman,
Chief Executive Officer and
Director

James G. Kaiser, Director

Theresa F. Yerkes

Eileen S. Kraus

Theresa F. Yerkes, Vice President
and Controller (Chief Financial
Officer and Chief Accounting
Officer)

Eileen S. Kraus, Director

Stillman B. Brown

Hugo E. Uytterhoeven

Stillman B. Brown, Director

Hugo E. Uytterhoeven, Director

Edgar R. Fiedler

Walter W. Williams

Edgar R. Fiedler, Director

Walter W. Williams, Director

Mannie L. Jackson

Kathryn D. Wriston

Mannie L. Jackson, Director

Kathryn D. Wriston, Director

FORM 10-K--ITEM 14(a) (1) and (2)

THE STANLEY WORKS AND SUBSIDIARIES

INDEX TO FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULES

The following consolidated financial statements and report of independent auditors of The Stanley Works and subsidiaries, included in the Annual Report of the Registrant to its Shareholders for the fiscal year ended January 3, 1998, are incorporated by reference in Item 8:

Report of Independent Auditors

Consolidated Statements of Operations--fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995.

Consolidated Balance Sheets--January 3, 1998 and December 28, 1996.

Consolidated Statements of Cash Flows--fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995.

Consolidated Statements of Changes in Shareholders' Equity--fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995.

Notes to Consolidated Financial Statements.

The following consolidated financial statement schedule of The Stanley Works and subsidiaries is included in Item 14(d):

F-4 Schedule II--Valuation and Qualifying Accounts

All other schedules for which provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted.

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in this Annual Report (Form 10-K) of The Stanley Works of our report dated January 29, 1998, included in the 1997 Annual Report to Shareholders of The Stanley Works.

Our audits also included the consolidated financial statement schedule of The Stanley Works listed in Item 14(a). This schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits. In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also consent to the incorporation by reference in the following registration statements of our report dated January 29, 1998, with respect to the consolidated financial statements incorporated herein by reference, and our report included in the preceding paragraph with respect to the consolidated financial statement schedule included in this Annual Report (Form 10-K) of The Stanley Works.

Registration Statement (Form S-8 No. 2-93025)
Registration Statement (Form S-8 No. 2-96778)
Registration Statement (Form S-8 No. 2-97283)
Registration Statement (Form S-8 No. 33-16669)
Registration Statement (Form S-3 No. 33-12853)
Registration Statement (Form S-3 No. 33-19930)
Registration Statement (Form S-8 No. 33-39553)
Registration Statement (Form S-8 No. 33-41612)
Registration Statement (Form S-3 No. 33-46212)
Registration Statement (Form S-3 No. 33-47889)
Registration Statement (Form S-8 No. 33-55663)
Registration Statement (Form S-8 No. 33-62565)
Registration Statement (Form S-8 No. 33-62567)
Registration Statement (Form S-8 No. 33-62575)

ERNST & YOUNG LLP

Hartford, Connecticut
March 26, 1998

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in the following registration statements pertaining to The Stanley Works 401(k) Savings Plan of our report dated March 13, 1998, with respect to the financial statements and schedules of The Stanley Works 401(k) Savings Plan for the year ended December 31, 1997 included as Exhibit 99(i) to this Annual Report (Form 10-K) for the fiscal year ended January 3, 1998.

Registration Statement (Form S-8 No. 2-97283)
Registration Statement (Form S-8 No. 33-41612)
Registration Statement (Form S-8 No. 33-55663)

ERNST & YOUNG LLP

Hartford, Connecticut
March 26, 1998

SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS

THE STANLEY WORKS AND SUBSIDIARIES

Fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995 (In Millions of Dollars)

| COL. A | COL. B | COL. C | | COL. D | COL. E |
|---|--------------------------------|--------------------------------------|---|-----------------------|--------------------------|
| Description | Balance at Beginning of Period | Additions | | Deductions - Describe | Balance at End of Period |
| | | (1) Charged to Costs and Expenses | (2) Charged to Other Accounts - Describe | | |
| Fiscal year ended January 3, 1998 | | | | | |
| Reserves and allowances deducted from asset accounts: | | | | | |
| Allowance for doubtful accounts: | | | | | |
| Current | \$22.5 | \$20.2 | (\$6.8)(B) | \$16.1 (A) | \$19.8 |
| Noncurrent | 0.8 | (0.2) | 0.1 (B) | | 0.7 |
| Fiscal year ended December 28, 1996 | | | | | |
| Reserves and allowances deducted from asset accounts: | | | | | |
| Allowance for doubtful accounts: | | | | | |
| Current | \$18.2 | \$21.1 | | \$16.8 (A) | \$22.5 |
| Noncurrent | 0.8 | | | | 0.8 |
| Fiscal year ended December 30, 1995 | | | | | |
| Reserves and allowances deducted from asset accounts: | | | | | |
| Allowance for doubtful accounts: | | | | | |
| Current | \$20.9 | \$9.7 | \$0.4(B) | \$12.8 (A) | \$18.2 |
| Noncurrent | 0.5 | 0.3 | | | 0.8 |

Notes: (A) Represents doubtful accounts charged off, less recoveries of accounts previously charged off.
(B) Represents net transfers to/from other accounts, foreign currency translation adjustments and acquisitions.

EXHIBIT LIST

- (3) (i) Restated Certificate of Incorporation
(incorporated by reference to Exhibit (3)(i) to
Quarterly Report on Form 10-Q for quarter ended
June 29, 1996)
- (ii) By-laws
- (4) (i) Indenture defining the rights of holders of 7-3/8%
Notes Due December 15, 2002 and 9% Notes due 1998
(incorporated by reference to Exhibit 4(a) to
Registration Statement No. 33-4344 filed March
27, 1986)
- (ii) First Supplemental Indenture, dated as of June 15, 1992
between the Company and Shawmut Bank Connecticut,
National Association (formerly known as The Connecticut
National Bank) (incorporated by reference to Exhibit
(4)(c) to Registration Statement No. 33-46212 filed
July 21, 1992)
- (a) Certificate of Designated Officers establishing
Terms of 9% Notes (incorporated by reference to
Exhibit (4)(i)(c) to Annual Report on Form 10-K for
year ended January 2, 1988)
- (b) Certificate of Designated Officers establishing
Terms of 7-3/8% Notes Due December 15, 2002
(incorporated by reference to Exhibit (4)(ii) to
Current Report on Form 8-K dated December 7, 1992)
- (iii) Rights Agreement, dated January 31, 1996 (incorporated
by reference to Exhibit (4)(i) to Current Report on
Form 8-K dated January 31, 1996)
- (iv)(a) Amended and Restated Facility A (364 Day) Credit
Agreement, dated as of October 23, 1996, with the
banks named therein and Citibank, N.A. as agent
(incorporated reference to Exhibit 4(iv) to Annual
Report on Form 10-K for year ended December 28, 1996)
- (b) Letter Agreement, dated October 22, 1997 regarding
the extension of the Amended and Restated Facility
A (364 Day) Credit Agreement.

- (v) Amended and Restated Facility B (Five Year) Credit Agreement, dated as of October 23, 1996, with the banks named therein and Citibank, N.A. as agent (incorporated reference to Exhibit 4(v) to Annual Report on Form 10-K for year ended December 28, 1996)
- (10) (i) Executive Agreements (incorporated by reference to Exhibit 10(i) to Annual Report on Form 10-K for year ended January 3, 1987)*
- (ii) Deferred Compensation Plan for Non-Employee Directors as amended January 31, 1996 (incorporated by reference to Exhibit 10(i) to Current Report on Form 8-K dated January 31, 1996)*
- (iii) 1988 Long-Term Stock Incentive Plan, as amended*
- (iv) Management Incentive Compensation Plan effective January 1, 1996 (incorporated by reference to Exhibit 10(iv) to Annual Report on Form 10-K for year ended December 30, 1995)*
- (v) Deferred Compensation Plan for Participants in Stanley's Management Incentive Plan effective January 1, 1996 (incorporated by reference to Exhibit 10(v) to Annual Report on Form 10-K for year ended December 30, 1995)*
- (vi) Supplemental Retirement and Savings Plan for Salaried Employees of The Stanley Works effective as of January 1, 1997*
- (vii) Term Loan Agreement dated as of May 13, 1988 between the Savings and Retirement Trust for Salaried Employees and Wachovia Bank and Trust Company N.A. and related Guaranty dated as of May 13, 1988 from The Stanley Works to Wachovia Bank and Trust Company, N.A. (incorporated by reference to Exhibit 10(x) to Annual Report on Form 10-K for year ended December 31, 1988)
- (viii) Loan and Guarantee Agreement dated as of June 6, 1989 among The Stanley Works Savings Trust for Hourly Paid Employees, The Stanley Works and Wachovia Bank and Trust Company, N.A., Massachusetts Mutual Life Insurance Company and The Lincoln National Life Insurance Company (incorporated by reference to Exhibit 10(i) to Quarterly Report on Form 10-Q for quarter ended July 1, 1989)

* Management contract or compensation plan or arrangement

(a) First Amendment to Loan and Guarantee Agreement dated as of February , 1993 (incorporated by reference to Exhibit 10(viii)(a) to Annual Report on Form 10-K for year ended December 31, 1994)

(ix) Loan and Guarantee Agreement dated as of June 6, 1989 among The Stanley Works Savings and Retirement Trust, The Stanley Works and Wachovia Bank and Trust Company, N.A., Massachusetts Mutual Life Insurance Company, The Lincoln National Life Insurance Company, First Penn-Pacific Life Insurance Company, Security-Connecticut Life Insurance Company-Universal Life, Lincoln National Life Reinsurance Company and American States Life Insurance Company-Universal Life (incorporated by reference to Exhibit (10)(ii) to Quarterly Report on Form 10-Q for quarter ended July 1, 1989)

(a) First Amendment to Loan and Guarantee Agreement dated as of February , 1993 (incorporated by reference to Exhibit 10(ix)(a) to Annual Report on Form 10-K for year ended December 31, 1994)

(x) Assignment and Assumption Agreement and Second Amendment to Loan and Guarantee Agreements, dated as of September 30, 1994, among The Stanley Works Savings Trust for Hourly Paid Employees, The Stanley Works Savings and Retirement Trust, The Stanley Works and the Financial Institutions named in Schedules I and II thereto (incorporated by reference to Exhibit 10(x) to Annual Report on Form 10-K for year ended December 31, 1994)

(xi) (a) Supplemental Executive Retirement Program effective May 20, 1997*

(b) Amendment to John M. Trani's Supplemental Executive Retirement Program, dated September 17, 1997*

(xii)(a) The Stanley Works Non-Employee Directors' Benefit Trust Agreement dated December 27, 1989 and amended as of January 1, 1991 by and between The Stanley Works and Connecticut National Bank (incorporated by reference to Exhibit (10)(xvii)(a) to Annual Report on Form 10-K for year ended December 29, 1990)

(b) The Stanley Works Employees' Benefit Trust Agreement dated December 27, 1989 and amended as of January 1, 1991 by and between The Stanley

* Management contract or compensation plan or arrangement

Works and Connecticut National Bank (incorporated by reference to Exhibit (10)(xvii)(b) to Annual Report on Form 10-K for year ended December 29, 1990)

- (xiii) Restated and Amended 1990 Stock Option Plan (incorporated by reference to Exhibit 10 (xiii) to Annual Report on Form 10-K for the year ended December 28, 1996)
- (xiv) Term Note, dated as of June 7, 1991, by State Street Bank and Trust Company, as Trustee for the Savings Plan for Salaried Employees of The Stanley Works, to Stanley Works Funding Corporation (incorporated by reference to Exhibit (10)(xxi) to Current Report on Form 8-K dated June 7, 1991)
- (xv) Term Note, dated as of June 7, 1991, by State Street Bank and Trust Company, as Trustee for the Savings Plan for Hourly Paid Employees of The Stanley Works, to Stanley Works Funding Corporation (incorporated by reference to Exhibit (10)(xxii) to Current Report on Form 8-K dated June 7, 1991)
- (xvi) Master Leasing Agreement, dated September 1, 1992 between BLC Corporation and The Stanley Works (incorporated by reference to Exhibit (10)(i) to Quarterly Report on Form 10-Q for quarter ended September 26, 1992)
- (xvii) The Stanley Works Stock Option Plan for Non-Employee Directors, as amended December 18, 1996
- (xviii) Employment Agreement effective December 27, 1996 between The Stanley Works and John M. Trani (incorporated by reference to Exhibit 10(i) to Current Report on Form 8-K dated January 2, 1997)*
- (xix) Employment Agreement effective December 31, 1996 between The Stanley Works and Richard H. Ayers (incorporated by reference to Exhibit 10(ii) to Current Report on Form 8-K dated January 2, 1997)*
- (xx) Letter Agreement, dated April 30, 1996 between The Stanley Works and Paul W. Russo *
- (xxi) 1997 Long-Term Incentive Plan*

* Management contract or compensation plan or arrangement

- (11) Statement re computation of per share earnings (the information required to be presented in this exhibit appears in footnote J to the Company's Consolidated Financial Statements set forth in the Annual Report to Shareholders for the year ended January 3, 1998)
- (12) Statement re computation of ratio of earnings to fixed charges
- (13) Annual Report to Shareholders for year ended January 3, 1998
- (21) Subsidiaries of Registrant
- (23) Consents of Independent Auditors (at pages F-2 and F-3)
- (27) Financial Data Schedule for 1997 Fiscal Year End
 - (i) Financial Data Schedule for 1997 interim periods and 1996 Fiscal Year End
 - (ii) Financial Data Schedule for 1996 interim periods and 1995 Fiscal Year End
- (99) (i) Financial Statements and report of independent auditors for the year ended December 31, 1997, of The Stanley Works 401(k) Savings Plan
 - (ii) Policy on Confidential Proxy Voting and Independent Tabulation and Inspection of Elections as adopted by The Board of Directors October 23, 1991 (incorporated by reference to Exhibit (28)(i) to Quarterly Report on Form 10-Q for quarter ended September 28, 1991)

EXHIBIT 3(ii)

THE STANLEY WORKS

BYLAWS

ARTICLE I

SHAREHOLDERS' MEETINGS

1. ANNUAL MEETING. The Annual Meeting of the shareholders shall be held at such time in the month of February, March or April in each year and at such place within or without the State of Connecticut as the Board of Directors may determine. Notice thereof shall be mailed to each shareholder to his or her last known post office address not less than twenty-five days nor more than fifty days before such Meeting.
2. SPECIAL MEETINGS. Special Meetings of the shareholders shall be called by the Chairman, or the President or Secretary, or by the Chairman, or the President or Secretary upon the written request of the holders of not less than 35% of the voting power of all shares entitled to vote on any issue proposed to be considered at such Meeting by mailing a notice thereof to each shareholder to his or her last known post office address not less than twenty-five days nor more than fifty days before such Meeting.
3. QUORUM. At any Meeting of shareholders the holders of not less than a majority of the shares outstanding and entitled to vote present in person or by proxy shall constitute a quorum. The Directors may establish a record date for voting or other purposes in accordance with law.
4. BUSINESS TO BE CONDUCTED AT ANNUAL MEETING. No business may be transacted at an Annual Meeting of shareholders (including any adjournment thereof), other than business that is either (a) specified in the notice of meeting (or any supplement thereto) given by or at the direction of the Board of Directors (or any duly authorized committee thereof), (b) otherwise properly brought before the Annual Meeting by or at the direction of the Board of Directors (or any duly authorized committee thereof) or (c) otherwise properly brought before the Annual Meeting by any shareholder (i) who is a shareholder of record on the date of the giving of the notice provided for in this Section 4 and on the record date for the determination of shareholders entitled to vote at such Annual Meeting and (ii) who

complies with the notice procedures set forth in this Section 4.

In addition to any other applicable requirements, for business to be properly brought before an Annual Meeting by a shareholder, such shareholder must have given timely notice thereof in proper written form to the Secretary.

To be timely, a shareholder's notice to the Secretary must be delivered to or mailed and received at the principal executive offices of the Corporation not less than sixty (60) days nor more than ninety (90) days prior to the anniversary of the date on which the immediately preceding Annual Meeting of shareholders was convened; provided, however, that in the event that the Annual Meeting is called for a date that is not within thirty (30) days before or after such anniversary date, notice by the shareholder in order to be timely must be so received not later than the close of business on the tenth (10th) day following the day on which such notice of the date of the Annual Meeting was mailed or such public disclosure of the date of the Annual Meeting was made, whichever first occurs.

To be in proper written form, a shareholder's notice to the Secretary must set forth as to each matter such shareholder proposes to bring before the Annual Meeting (i) a brief description of the business desired to be brought before the Annual Meeting and the reasons for conducting such business at the Annual Meeting, (ii) the name and record address of such shareholder, (iii) the class or series and number of shares of capital stock of the Corporation which are owned beneficially or of record by such shareholder, (iv) a description of all arrangements or understandings between such shareholder and any other person or persons (including their names) in connection with the proposal of such business by such shareholder and any material interest of such shareholder in such business and (v) a representation that such shareholder intends to appear in person or by proxy at the Annual Meeting to bring such business before the meeting.

No business shall be conducted at the Annual Meeting of shareholders except business brought before the Annual Meeting in accordance with the procedures set forth in this Section 4, provided, however, that, once business has been properly brought before the Annual Meeting in accordance with such procedures, nothing in this Section 4 shall be deemed to preclude discussion by any shareholder of any such business. If the Chairman of an Annual Meeting determines that business was not properly brought before the Annual Meeting in accordance with the foregoing procedures, the Chairman shall declare to the meeting that the business was not properly brought before the meeting and such business shall not be transacted.

ARTICLE II

NOMINATIONS OF DIRECTOR CANDIDATES

1. ELIGIBILITY TO MAKE NOMINATIONS. Nominations of candidates for election as directors of the Corporation at any meeting of shareholders called for election of directors (an "Election Meeting") may be made by the Board of Directors or by any shareholder entitled to vote at such Election Meeting.
2. PROCEDURE FOR NOMINATIONS BY THE BOARD OF DIRECTORS. Nominations made by the Board of Directors shall be made at a meeting of the Board of Directors, or by written consent of directors in lieu of a meeting, not less than 30 days prior to the date of the Election Meeting, and such nominations shall be reflected in the minute books for the Corporation as of the date made. At the request of the Secretary of the Corporation each proposed nominee shall provide the Corporation with such information concerning himself or herself as is required, under the rules of the Securities and Exchange Commission, to be included in the Corporation's proxy statement soliciting proxies for his or her election as a director.
3. PROCEDURE FOR NOMINATIONS BY SHAREHOLDERS. Not less than 30 days prior to the date of the Election Meeting, any shareholder who intends to make a nomination at the Election Meeting shall deliver a notice to the Secretary of the Corporation setting forth (i) the name, age, business address and residence address of each nominee proposed in such notice, (ii) the principal occupation or employment of each such nominee, (iii) the number of shares of capital stock of the Corporation which are beneficially owned by each such nominee and (iv) such other information concerning each such nominee as would be required, under the rules of the Securities and Exchange Commission, in a proxy statement soliciting proxies for the election of such nominees.
4. SUBSTITUTION OF NOMINEES. In the event that a person is validly designated as a nominee in accordance with section 2 or 3 hereof and shall thereafter become unable or unwilling to stand for election to the Board of Directors, a substitute nominee may be designated as follows:
 - (a) by those named as proxies in proxies solicited on behalf of the Board of Directors if the person was designated as nominee in accordance with section 2 hereof
 - (b) by the shareholder who proposed such nominee if the person was designated as a nominee in accordance with section 3 hereof.

5. DETERMINATION OF COMPLIANCE WITH PROCEDURE.
If the chairman of the Election Meeting determines that a nomination was not in accordance with the foregoing procedures, such nomination shall be void.

ARTICLE III

DIRECTORS AND COMMITTEES

1. DIRECTORS. The business, property and affairs of this Corporation shall be managed by or under the direction of the Board of Directors consisting of not less than nine nor more than eighteen Directors, the exact number to be determined by the Board of Directors from time to time. All Directors shall be shareholders of record. The Directors shall be divided into three classes designated Class I, Class II and Class III. Such classes shall be as nearly equal in number as the total number of Directors constituting the entire Board of Directors permits. One class shall be chosen annually at the Annual Meeting of shareholders and the members of such class shall hold office until their successors be elected and qualified. The Directors may increase the prescribed number of Directors by the concurring vote of a majority of the prescribed number of Directors. Any increase or decrease in the prescribed number of Directors shall be so apportioned among the classes of Directors as to make all the classes as nearly equal in number as possible. No reduction of the number of Directors shall remove or shorten the term of any Director in office. A majority of the number of Directors prescribed shall constitute a quorum for the transaction of business.
2. MEETINGS. The Chairman or the President or any Vice Chairman may and upon written application of any three Directors shall call a meeting of the Board of Directors to be held at such time and place as may be determined by the person calling said meeting and shall cause notice thereof to be given. Unless waived in writing, three days verbal or written (mail) notice shall be required provided, however, that if in the judgment of any two officers an emergency exists, a meeting may be called forthwith by telephone or telegram or verbal notice and such notice shall be deemed sufficient notice notwithstanding that some of the Directors may not have actual notice.
- The Annual Meeting of the Directors for the election of officers shall be held without notice, immediately after the Annual Meeting of shareholders. Regular meetings of the Directors shall be held at least on a quarterly basis.
3. WRITTEN CONSENT. If all the Directors, or all members of a committee of the Board of Directors, as the case may be, severally or collectively consent in writing to any action taken or to be taken by the Corporation, and the number of such Directors or members

constitutes a quorum for such action, such action shall be a valid corporate action as though it had been authorized at a meeting of the Board of Directors or committee, as the case may be. The Secretary shall file such consents with the minutes of the Board of Directors or of the committee, as the case may be.

4. PARTICIPATION BY TELEPHONE. A Director may participate in a meeting of the Board of Directors or of a committee by any means of communication by which all Directors participating in the meeting may simultaneously hear one another during the meeting, and participation in a meeting pursuant to this subsection shall constitute presence in person at such meeting.

5. VACANCIES. In case any vacancy or vacancies shall exist in the Board of Directors at any time the remaining members of the Board by majority action may fill the vacancy or vacancies. The term of a Director elected to fill a vacancy expires at the next shareholders meeting at which Directors are elected.

6. COMMITTEES. The Board of Directors may from time to time appoint from its membership such committees as it may deem necessary or desirable for the best interests of the Corporation and may delegate to any committee all needful authority to the extent permitted by law.

Each committee shall fix its own rules as to procedure and calling of meetings. It shall appoint a Secretary, who need not be a member of the committee. Such Secretary shall call meetings of the committee on the request of the Chair of the committee or any two members and shall keep permanent record of all of its proceedings. A majority of the members of any committee shall constitute a quorum.

7. EXECUTIVE COMMITTEE. The Directors shall appoint an Executive Committee consisting of the Chairman, if any, the President and at least three other Directors, but in no event shall the Committee consist of less than five members. The Board of Directors may at any time decrease (subject to the provisions of the preceding paragraph) or increase the size of said Committee, may change the membership thereof and may fill vacancies therein.

During intervals between meetings of the Board of Directors, the Executive Committee shall possess and may exercise all the powers of the Board of Directors in the management of the business and affairs of the Corporation, but the Committee shall have no power to declare dividends or do other things specially reserved by law to the Directors. The Executive Committee shall have power to appoint such subcommittees as it may deem necessary to report and make recommendations to the Executive Committee. Any action taken by the Executive Committee shall be subject to change, alteration and

revision by the Board of Directors, provided that no rights or acts of others shall be affected by any such alteration or revision.

8. FINANCE AND PENSION COMMITTEE. A Finance and Pension Committee consisting of at least five Directors shall be appointed by the Board of Directors. The Committee shall advise and assist the Chief Financial Officer and the Treasurer in major matters concerning the finances of the Corporation and in matters of major policy decisions in the purchase and sale of securities. In performance of this the Committee shall regularly review the financial condition of the Corporation so as to counsel these officers and the Board on the total financial resources, strength and capabilities of the Corporation. In this connection, the Committee shall analyze and advise on fundamental corporate changes in capital structure (both debt and equity); review the capital structure of the Corporation and make recommendations with respect to management proposals concerning financing, purchases of treasury stock, investments, and dividend actions; review periodically the Corporation's risk management program and its adequacy to safeguard the Corporation against extraordinary liabilities or losses; and advise and assist in matters such as short-term investments, credit liabilities, financings, and hedges of foreign currency exposures.

The Committee shall oversee the Corporation's administration of its pension plans and of the pension plans of its subsidiaries. The Committee shall be responsible for setting (subject to the approval of the Board of Directors) the retirement policies of the Corporation and its subsidiaries; for amending pension plans, savings and retirement plans, stock ownership plans or any similar plans or related trust agreements; and for approving actuarial assumptions and investment policies for the Corporation's pension plans. It shall report at least annually to the Board of Directors. The Committee may delegate any or all of these functions to such employees as it, in its judgment, deems appropriate.

Specifically, the Committee shall approve retaining or terminating the services of actuaries, lawyers, accountants or other professionals for the plans; shall approve annually the amount of the contributions to be made by the Corporation to the respective plans; and shall approve appointing and terminating trustees and investment managers and determine the allocation of the assets of the plans among one or more trustees or investment managers.

9. AUDIT COMMITTEE. An Audit Committee consisting of at least three Directors, none of whom shall be officers or employees of the Corporation or any of its subsidiaries, shall be appointed by the Board of Directors. The Committee shall nominate the public accounting firm to conduct the annual audit and shall review fees for audit and tax work and approve in advance management consulting services which management may

propose be provided by the Corporation's public accounting firm. With respect to such management consulting services, consideration shall be given to the effect that performing such services might have on audit independence. The Committee shall review with the auditors the scope and timing of their audit examination, with particular emphasis on those areas which either the Committee or the auditors believe warrant special attention. The Committee is authorized to have the auditors perform such supplemental reviews or audits as it deems desirable.

The Committee shall review the audited financial statements and the auditors' report thereon, including consideration of all significant disclosures required by the Securities and Exchange Commission, and any proposed changes in accounting principles or practices which have a significant impact on amounts reported for the current year (or will have in the future) and shall discuss with the auditors any significant problems encountered in the completion of the audit. The Committee shall review with management and the independent auditors the qualitative judgments about the appropriateness, not just the acceptability, of accounting principles and financial disclosure practices used or proposed to be adopted including the degree of aggressiveness or conservatism of the accounting principles and underlying estimates including significant liabilities and reserves associated with those liabilities. The Committee shall review the auditors' recommendations regarding internal control and their comments, if any, relating to conflicts of interest, questionable payments or other similar matters, and monitor with management the consideration given and/or the corrective action taken with respect to these comments and recommendations. The Committee shall review management's evaluation of the Corporation's system of internal accounting controls, including the independence, scope and results of the internal audit function, and monitor the effectiveness of the system with management, independent auditors and internal audit management. The Committee shall review with management and independent auditors and consider the impact on the Corporation of significant recent or pending statements by the Financial Accounting Standards Board, the Securities and Exchange Commission, the Auditing Standards Executive Committee of the American Institute of Certified Public Accountants and similar authoritative bodies. The Committee shall review environmental liabilities and the reserves associated with those liabilities.

In carrying out all of the foregoing responsibilities, the Committee shall have direct and open access to Management, public accountants and internal audit management (each of which shall have direct and open access to the Committee); shall submit Committee reports, recommendations, and minutes of meetings to the Board of Directors; and shall provide opportunities to the other members of the Board to have full and open access to the independent auditors.

10. COMPENSATION AND ORGANIZATION COMMITTEE. A Compensation and Organization Committee consisting of at least three Directors, none of whom shall be employees of the Corporation or any of its subsidiaries, shall be appointed by the Board of Directors. The Committee shall review and approve major organization and compensation structure changes as recommended by Management. Although the Board, itself, will review the performance of the chief executive officer and fix his or her salary, the Committee shall approve the performance and determine the salaries of the other executive officers of the Corporation and of other senior executives whose base salary exceeds an amount fixed by the Board of Directors; shall determine the compensation of all executive officers and such senior executives under the Corporation's senior executive compensation plans; shall administer all of the Corporation's senior executive compensation plans; and shall assure that there is a succession plan in place.

11. COMMITTEE ON BOARD AFFAIRS AND PUBLIC POLICY. A Committee on Board Affairs and Public Policy consisting of at least three directors, none of whom shall be employees of the Corporation or any of its subsidiaries shall be appointed by the Board of Directors. The Committee shall consider and make recommendations to the Board of Directors as to Board of Director membership with respect to names generated by the Committee itself or submitted by shareholders. The Committee shall consider and make recommendations to the Board of Directors with respect to Board of Director committee membership and chair assignments. (These will normally be acted upon by the Board of Directors at its Annual Meeting held immediately after the Annual Meeting of shareholders.) The Committee shall consider and make recommendations to the Board of Directors with respect to the number of members of the Board of Directors. (The Charter and Bylaws provide for not less than nine nor more than eighteen as may be determined by the Board). Annually, the Committee shall consider and recommend to the Board of Directors the persons whom the Committee proposes that the Board of Directors nominate for election as directors at the Annual Meeting of shareholders. The Committee shall consider and make recommendations to the Board of Directors with respect to remuneration of directors.

The Committee shall provide guidance to the Management on major issues in areas of corporate social responsibility, including environmental issues and public affairs. The Committee shall review and approve policy guidelines to be used by Management in making charitable contributions and shall annually review all charitable contributions made by the Corporation during the previous twelve months and recommend to the Board the level of contributions to be set for the ensuing year.

12. In the absence of any one or more members from a meeting of any of the committees provided for in these Bylaws, the Chairman, or the President, may in his or her discretion invite any member or members of the Board (otherwise qualified to serve) to attend such

meeting. Temporary members thus appointed to attend for absentees shall act as regular members and shall have the right to vote.

13. POWERS OF ALL COMMITTEES. The powers of all committees are at all times subject to the control of the Directors, and any member of any committee may be removed at any time at the pleasure of the Board.

ARTICLE IV

OFFICERS

1. ELECTION OF OFFICERS. The Board of Directors shall have power to elect from its own members or otherwise a Chairman, a President, one or more Vice Chairmen and Vice Presidents, a Secretary, a Treasurer, one or more Assistant Treasurers and Assistant Secretaries, and such other officers, agents and employees as it may deem expedient, and to define the duties and authority of all officers, employees and agents and to delegate to them such lawful powers as may be deemed advisable.

The officers shall respectively perform all acts and duties required of such officers by law, by the Charter and Bylaws of this Corporation, or by the Board of Directors.

2. CHAIRMAN OF THE BOARD. If the Directors have elected a Chairman, the Chairman shall preside at all meetings of the Board except that in the Chairman's absence the Directors present shall designate a person to preside. The Chairman shall have such additional duties as the Board of Directors or the Executive Committee may assign.
3. PRESIDENT. The President shall be elected by the Directors and shall have such duties as the Board of Directors or the Executive Committee may assign.
4. CHIEF EXECUTIVE OFFICER. One of the officers shall be appointed Chief Executive Officer of the Corporation by the Board of Directors. Subject to the Board of Directors and the Executive Committee, the Chief Executive Officer shall have general supervision and control of the policies, business and affairs of the Corporation.
5. VICE CHAIRMEN. Each Vice Chairman shall have such powers and perform such duties as may be conferred upon him or her or determined by the Chief Executive Officer.
6. VICE PRESIDENTS. Each Vice President shall have such powers and perform such duties as may be conferred upon him or her or determined by the Chief Executive Officer.

7. TREASURER. The Treasurer shall have the oversight and control of the funds of the Corporation and shall have the power and authority to make and endorse notes, drafts and checks and other obligations necessary for the transaction of the business of the Corporation except as herein otherwise provided.
8. CONTROLLER. The Controller shall have the oversight and control of the accounting records of the Corporation and shall prepare such accounting reports and recommendations as shall be appropriate for the operation of the Corporation.
9. SECRETARY. It shall be the duty of the Secretary to make and keep records of the votes, doings and proceedings of all meetings of the shareholders and Board of Directors of the Corporation, and of its Committees, and to authenticate records of the Corporation.
10. ASSISTANT TREASURERS. The Assistant Treasurers shall have such duties as the Treasurer shall determine.
11. ASSISTANT SECRETARIES. The Assistant Secretaries shall have such duties as the Secretary shall determine.
12. POWERS OF ALL OFFICERS. The powers of all officers are at all times subject to the control of the Directors, and any officer may be removed at any time at the pleasure of the Board.

ARTICLE V
INDEMNIFICATION

To the extent properly permitted by law the Board of Directors shall provide for the indemnification and reimbursement of, and advances of expenses to, any person made a party to any action, suit or proceeding by reason of the fact that he or she, or a person whose legal representative or successor he or she is,

- (a) is or was a Director, officer, employee or agent of the Corporation, or
- (b) served at the Corporation's request as a director, officer, employee or agent of another corporation, for expenses, including attorney's fees, and such amount of any judgment, money decree, fine, penalty or settlement for which he or she may have become liable as the Board of Directors deems reasonable, actually incurred by him or her in connection with the defense or reasonable settlement of any such action, suit or

proceeding or any appeal therein, except in relation to matters as to which he or she, or such person whose legal representatives or successor he or she is, is finally adjudged in such action, suit or proceeding to be liable for negligence or misconduct in the performance of his or her duties.

This provision of indemnification shall be in addition to any other right or remedy which such person may have. The Corporation shall have the right to intervene in and defend all such actions, suits or proceedings brought against any such person.

ARTICLE VI
CORPORATE SEAL

The corporate seal shall be in the custody of the Secretary and either the Secretary or any other officer shall have the power to affix the same for the Corporation.

ARTICLE VII
STOCK CERTIFICATES

1. SIGNATURES. Certificates of stock shall be signed by the Chairman, the President or a Vice President and by the Secretary or the Treasurer (except that where any such certificate is signed by a transfer agent or transfer clerk and by the registrar, the signatures of any such Chairman, President, Vice President, Secretary or Treasurer may be facsimiles, engraved or printed) and shall be sealed with the seal of the corporation (or shall bear a facsimile of such seal).
2. LOST CERTIFICATES. No certificate for shares of stock in the Corporation shall be issued in place of any certificate alleged to have been lost, stolen or destroyed except upon production of such evidence of such loss, theft or destruction as the Board of Directors in its discretion may require and upon delivery to the Corporation of a bond of indemnity in form and, unless such requirement is waived by Resolution of the Board, with one or more sureties, satisfactory to the Board in at least double the value of the stock represented by said Certificate.

ARTICLE VIII

FISCAL YEAR

The Corporation's fiscal year shall close on the Saturday nearest December 31st of each year.

ARTICLE IX

INDEPENDENT AUDIT

The Board of Directors shall provide for a yearly independent audit, the form and scope of which shall be determined by the Board from time to time.

ARTICLE X

AMENDMENTS

The Board of Directors of the Corporation may adopt, amend or repeal the Bylaws of the Corporation, subject, however, to the power of the shareholders to adopt, amend or repeal the same, provided that any notice of a meeting of shareholders or of the Board of Directors at which Bylaws are to be adopted, amended or repealed, shall include notice of such proposed action.

ARTICLE XI

ACQUISITIONS OF STOCK

- (a) Except as set forth in subsection (b) hereof, the Corporation shall not acquire any of its voting equity securities (as defined below) at a price per share above the market price per share (as defined below) of such securities on the date of such acquisition from any person actually known by the Corporation to be the beneficial owner (as determined pursuant to Rule 13d-3 under the Securities Exchange Act of 1934, as amended, or any successor rule or regulation) of more than three percent of the Corporation's voting equity securities who has been the beneficial owner of the Corporation's voting equity securities for less than two years prior to the date of the Corporation's acquisition thereof, unless such acquisition (i) has been approved by a vote of a majority of the shares entitled to vote, excluding shares owned by any beneficial owner any of whose shares are proposed to be acquired pursuant to the proposed acquisition that is the subject of such vote or (ii) is pursuant to an offer made on the same terms to all holders

of securities of such class. The determination of the Board of Directors shall be conclusive in determining the price paid per share for acquired voting equity securities if the Corporation acquires such securities for consideration other than cash.

- (b) This provision shall not restrict the Corporation from: (i) acquiring shares in the open market in transactions in which there has been no prior arrangement with, or solicitation of (other than a solicitation publicly made to all holders), any selling holder of voting equity securities or in which all shareholders desiring to sell their shares have an equal chance to sell their shares; (ii) offering to acquire shares of shareholders owning less than 100 shares of any class of voting equity securities; (iii) acquiring shares pursuant to the terms of a stock option or similar plan that has been approved by a vote of a majority of the Corporation's common shares represented at a meeting of shareholders and entitled to vote thereon; (iv) acquiring shares from, or on behalf of, any employee benefit plan maintained by the Corporation or any subsidiary or any trustee of, or fiduciary with respect to, any such plan when acting in such capacity; or (v) acquiring shares pursuant to a statutory appraisal right or otherwise as required by law.
- (c) Market price per share on a particular day means the highest sale price on that day or during the period of five trading days immediately preceding that day of a share of such voting equity security on the Composite Tape for New York Stock Exchange-Listed Stocks, or if such voting equity security is not quoted on the Composite Tape on the New York Stock Exchange or listed on such Exchange, on the principal United States securities exchange registered under the Securities Exchange Act of 1934 on which such voting equity security is listed, or, if such voting equity security is not listed on any such exchange, the highest sales price or, if sales price is not reported, the highest closing bid quotation with respect to a share of such voting equity security on that day or during the period of five trading days immediately preceding that day on the National Association of Securities Dealers, Inc. Automated Quotations System or any system then in use, or if no such quotations are available, the fair market value on the date in question of a share of such voting equity security as determined by a majority of the Board of Directors.
- (d) Voting equity securities of the Corporation means equity securities issued from time to time by the Corporation which by their terms are entitled to be voted generally in the election of the directors of the Corporation.
- (e) The Board of Directors shall have the power to interpret the terms and provisions of, and make any determinations with respect to, this Article XI, which interpretations and determinations shall be conclusive.

October 22, 1997

The Stanley Works
1000 Stanley Drive
New Britain, CT 06053
Attention: Craig Douglas

Ladies and Gentlemen:

Reference is made to The Stanley Works' 364-Day Credit Agreement, dated as of October 23, 1996 (as amended, modified or supplemented from time to time, the "Credit Agreement," the terms defined therein being used herein as therein defined), among the undersigned, certain Lenders parties thereto, and Citibank, N.A., as agent for said Lenders.

This letter is to confirm on behalf of all the Lenders that, effective on October 22, 1997, the Termination Date is extended to October 21, 1998. Except as expressly provided herein, the Credit Agreement shall remain unchanged and in full force and effect.

Very truly yours,

CITICORP SECURITIES, INC.

By: Anita J. Brickell

Title: Vice President

CITIBANK, N.A.

By: Steven R. Victorin

Title: Attorney-In-Fact

ACCEPTED AND AGREED
this 23rd day of October, 1997:

THE STANLEY WORKS

By: Craig A. Douglas

Title: Director, Corporate Finance

As amended January 28, 1998

THE STANLEY WORKS
1988 LONG-TERM STOCK INCENTIVE PLAN

1. PURPOSE

The purpose of The Stanley Works (the "Company") 1988 Long-Term Stock Incentive Plan (the "Plan") are to enhance and reinforce the Company's goals for profitable growth by providing senior management employees with additional financial rewards for attainment of such growth and encouraging their stock ownership through the payment of such rewards partly in Company stock.

2. DEFINITIONS

(A) The following terms shall have the following meanings for purposes of the Plan:

"Award Cycle" means the period over which the Target Incentive Award is to be earned out.

"Board of Directors" means the Board of Directors of The Stanley Works.

"Committee" means the Compensation and Organization Committee of the Board of Directors.

"Company" means The Stanley Works and each of its majority owned subsidiaries.

"Earnings Per Share" means the earnings per common share (on a fully diluted basis, if earnings per share are so reported) in the audited consolidated earnings statement for the year included in the Company's Annual Report to Stockholders.

"Net Earnings" means the net earnings in the audited consolidated statements of earnings for the year included in the Company's Annual Report to Stockholders.

"Participant" means any employee of the Company with respect to whom a Target Incentive Award is made.

"Target Incentive Award" means an award, expressed as a percentage of base salary,

assigned to a Participant to be earned out during the Award Cycle.

(B) Except when otherwise indicated by the context, any masculine terminology used herein shall also include the feminine and the definition of any terms herein in the singular shall also include the plural.

3. ADMINISTRATION

The Plan shall be administered by the Compensation and Organization Committee of the Board of Directors. The Committee is authorized to interpret the Plan and may, from time to time, adopt such rules and regulations for carrying out the Plan as it shall determine, provided the same are not inconsistent with the Plan as written. Decisions of the Committee shall be final, conclusive and binding on all parties.

4. PARTICIPATION

Participation in the Plan shall be limited to regular senior management employees of the Company, including officers, as specified by the Committee. The selection of Participants and their respective Target Incentive Awards shall be determined by the Committee.

5. AWARD GRANTS

(A) The Plan shall have a duration of ten fiscal years of the Company commencing January 3, 1988. Target Incentive Award grants will be made annually. Such awards will be paid out in full or in part on the basis of Company performance in terms of (i) in the case of Award Cycles commencing prior to January 1, 1989, compound annual growth rate in Earnings Per Share over a five-year Award Cycle, and (ii) in the case of Award Cycles commencing on or after January 1, 1989, average annual growth rate in Net Earnings over a five-year Award Cycle.

(B) Target Incentive Awards shall be expressed as a percentage of a Participant's average annual base salary (or, at the discretion of the Committee in the case of any or all Participants outside the United States, as a percentage of an amount deemed by the Committee appropriate to the Participant's position) during the Award Cycle with base salary calculated as zero for any portion of the Award Cycle that the employee is not a participant. In its discretion, the Committee may during an Award Cycle increase or decrease on a pro rata basis a Participant's Target Incentive Award percentage for that Award Cycle; if it does so, or if it establishes a Participant's Target Incentive Award for an Award Cycle at a higher or lower percentage than it had previously established for Award Cycles then underway, the Participant's Target Incentive Award percentage for all Award Cycles then underway shall be similarly

adjusted on a pro rata basis unless the Committee declares otherwise. Notwithstanding the foregoing sentence, there shall be no "decrease" nor "lower percentage" with respect to any Participant's participation in any particular Award Cycle except when such participation commenced on or after June 1, 1988. Notwithstanding the two immediately preceding sentences, there shall be no "decrease" nor "lower percentage" made by the Committee after any Change in Control of the Company (as defined in paragraph 13 hereof) with respect to any Participant's participation in any Award Cycle.

(C) Employees who become eligible to participate in the Plan during an Award Cycle may, at the discretion of the Committee, either be given a Target Incentive Award in such Award Cycle or be withheld from participation in the Plan until the beginning of the next Award Cycle. When the Committee designates an employee a Participant, such employee shall thereupon participate in all Award Cycles then underway.

6. RIGHT TO PAYMENT OF AWARDS

(A) The Committee shall, subject to approval by the Board of Directors, establish, prior to each Award Cycle, a targeted compound annual growth rate in Earnings Per Share (in the case of Award Cycles commencing prior to January 1, 1989) or in Net Earnings (in the case of Award Cycles commencing on or after January 1, 1989) at which 100% of the Target Incentive Award shall be earned. Such action by the Committee may be postponed until after the commencement of the Award Cycle, but in no event shall the Committee act more than six months after such commencement. The Committee shall also establish performance levels above and below this targeted level at which greater or lesser portions, respectively, of the Target Incentive Award shall be earned.

(B) Target Incentive Awards shall be earned and payable only if and to the extent to which actual Company performance meets or exceeds the minimum performance level established by the Committee.

(C) In an unusual circumstance, including but not limited to an acquisition, disposition or merger, stock split or stock dividend, or changes in accounting principles and methods, the Committee may make commensurate adjustments in performance levels during the Award Cycle.

7. PAYMENT OF AWARDS

(A) Except as otherwise provided in paragraph 9 hereof, no payment of Target Incentive Awards shall be made prior to the end of an Award Cycle.

(B) Payment of the Target Incentive Awards shall be made on the first business day of

April following the end of the last year of the Award Cycle, or such shorter period with respect to which payment shall be made pursuant to paragraph 9 hereof.

(C) Target Incentive Awards earned shall be paid fifty-five percent (55%) in cash and forty-five percent (45%) in shares of Company common stock or, at the discretion of the Committee, solely in cash, solely in shares or in any combination thereof. For purposes of determining the number of shares to be issued, the value per share shall be deemed to be the average of the daily closing prices of the common shares as reported for the New York Stock Exchange Composite Transactions during the Award Cycle.

8. DEFERRAL OF PAYMENT OF AWARDS

(A) Election by Participant.

(i) A Participant can elect to defer all or none of the Target Incentive Award payment. The election to defer by the Participant must be made not later than the December immediately preceding the last year of the Award Cycle whose Target Incentive Award payment is being deferred.

(ii) Once made, an election may not be changed either as to deferment or so as to accelerate the time of future payment, except (a) with the approval of the Committee upon demonstration of a financial hardship by the Participant, or (b) upon forfeiture of a penalty equal to that percentage of the amount of the payment equal to the Treasury Bill rate as provided in paragraph 8(D)(vi) hereof.

(iii) The election must specify when or under what circumstances the future lump-sum payment is to be made. The circumstances which may be specified are limited to death, retirement, or termination of employment.

Notwithstanding the specifics of the election, any deferred amount and earnings thereon not paid out prior to the later of the death of the Participant or the tenth anniversary of the Participant's termination of employment by death, retirement or otherwise will be paid out promptly after the later of such death or such anniversary.

(B) Participant's Account. Amounts which a Participant has elected to defer under the Plan shall be credited to the Participant's account in shares of the Corporation's common stock (valued at the mean between the highest and lowest sales prices of the common stock reported as New York Stock Exchange Composite Transactions for the date such amount would otherwise have been paid). The Participant shall not have any interest in the common stock until distributed in accordance with the Plan. Shares credited to the Participant's account shall accrue

amounts equivalent to cash or stock dividends. Such amounts shall similarly be credited to the Participant's account in shares of the Corporation's common stock valued as described in the first sentence of this paragraph as of the respective dividend payment dates.

(C) Distribution from Accounts.

(i) Distribution will be made from a Participant's account in January of the year specified in the election, but not later than promptly following the later of the death of the Participant or the tenth anniversary of a Participant's termination of employment by death, retirement or otherwise. Payment, subject to government withholding requirements, will be in the form of a stock certificate evidencing shares as follows:

- (a) the number of shares (adjusted as provided in paragraph 8 (D) (v) hereof for stock splits, etc.) the Participant would have received if his or her Target Incentive Award payment had not been deferred, plus
- (b) the number of shares representing the balance of his or her account (valued at the mean between the highest and lowest sales prices of the common stock reported as New York Stock Exchange Composite Transactions for the last trading day immediately preceding the date of payment).

(ii) The Committee may distribute all of a Participant's account prior to the date set forth in the Participant's election or elections in the event of an extraordinary corporate event or transaction.

(D) General.

(i) Dividends and other earnings credited on deferred amounts under the Plan will not constitute earnings for pension plan purposes.

(ii) The right of a Participant to receive any amount in the Participant's account shall not be transferable or assignable by the Participant, except by will or by the laws of descent and distribution, and no part of such amount shall be subject to attachment or other legal process.

(iii) The Company shall not be required to reserve or otherwise set aside shares of common stock for the payment of its obligations hereunder. The Company shall make available as and when required a sufficient number of shares of common stock to meet the needs of the Plan. To the extent that registration of

such shares under the Securities Act of 1933 shall be required prior to their resale, the Company undertakes to either file a registration statement relating to such shares or include such shares in another registration statement to be filed within a reasonable time.

(iv) Each Participant participating in the Plan will receive an annual statement indicating the number of shares credited to the Participant's account as of the end of the preceding calendar year.

(v) If adjustments are made to outstanding shares of common stock or to the capital structure of the Company as a result of stock dividends, stock splits or combinations, recapitalizations, mergers, consolidations, exchange offers, issuer tender offers, extraordinary cash dividends, or similar events or transactions, an appropriate adjustment will also be made in the number of shares credited to the Participant's account.

(vi) The Treasury Bill rate means that interest rate equal to the yield for 3- month U.S. Treasury Bills as reported for the last business day of the preceding calendar quarter.

9. TERMINATION OF EMPLOYMENT

(A) If a Participant's employment is terminated before the end of an Award Cycle for any reason other than death, total and permanent disability (as determined under the Company's pension plan) or retirement (normal or early), the rights of such Participant under the Plan shall terminate except as the Committee may in its discretion otherwise determine.

(B) If a Participant's employment is terminated before the end of an Award Cycle but not less than twelve (12) months after the start of such cycle on account of death, total and permanent disability (as determined under the Company's pension plan) or retirement (normal or early), or, if the Committee in the exercise of its discretion under (A) above shall have determined that the Participant's rights shall not terminate upon the termination of his employment, such Participant shall be entitled to a pro rata portion of any Target Incentive Award which would have been earned if the participant had continued employment through the end of the Award Cycle. Such pro rata portion shall be the arithmetic mean of the percentages of the Target Incentive Awards paid in respect of the four Award Cycles most recently completed prior to termination. The pro rata portion of the Award to which the Participant shall be entitled shall be calculated by multiplying the Target Incentive Award which would have been earned by a fraction, the numerator of which is the number of full months of participation in the Award Cycle and the denominator of which is the number of full months in the Award Cycle.

10. MISCELLANEOUS PROVISIONS

(A) Nothing in this Plan shall be construed as giving an employee any right to remain in the employ of the Company. The receipt of a Target Incentive Award grant for any one Award Cycle shall not give an employee a right to receive a Target Incentive Award grant for any subsequent Award Cycle.

(B) No right or interest of any Participant in the Plan shall be assignable or transferable, or subject to any lien, directly, by operation of law, or otherwise, including execution, levy, garnishment, attachment, pledge, and bankruptcy. In the event of a Participant's death, payment shall be made to the Participant's designated beneficiary, or in the absence of such designation, to the Participant's estate.

(C) The Company shall have the right to deduct from all payments under this Plan any Federal or state taxes required by law to be withheld with respect to such payments.

(D) Payments under the Plan shall not constitute earnings for purposes of the Company's pension plan.

(E) The number of shares which may be issued under this Plan subject to appropriate adjustment in the event of a stock dividend or stock split shall not exceed 1,400,000. In the event a greater number of shares would be required to satisfy Target Incentive Awards previously made, payment of such Awards may be made entirely in cash.

11. AMENDMENT AND TERMINATION

The Board of Directors may, at any time, terminate, modify or amend this Plan except insofar as the maximum number of shares to be issued hereunder is concerned. No termination, modification or amendment shall, without the consent of the Participants, adversely affect the rights of such Participants.

12. EFFECTIVE DATE OF THE PLAN

Subject to the approval of the shareholders of the Company, the Plan shall be effective as of January 3, 1988.

13. DEFINITION OF CHANGE IN CONTROL

For purposes of this Plan, a "Change in Control of the Company" shall be deemed to have occurred if

(A) Any "person", as such term is defined in Section 3 (a) (9) and modified and used in Section 13 (d) and 14 (d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") (other than the Company, any trustee or other fiduciary holding securities under an employee benefit plan of the Company (or of any subsidiary of the Company), or any corporation owned, directly or indirectly, by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company), is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 25% or more of the combined voting power of the Company's then outstanding securities;

(B) during any period of two consecutive years (not including any period prior to the adoption of this amendment to this Plan), individuals who at the beginning of such period constitute the Board, and any new director (other than a director designated by a person who has entered into an agreement with the Company to effect a transaction described in clause (A), (C) or (D) of this definition) whose election by the Board or nomination for election by the Company's stockholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors at the beginning of the period or whose election or nomination for election was previously so approved, cease for any reason to constitute at least a majority thereof;

(C) the stockholders of the Company approve a merger or consolidation of the Company with any other Corporation, other than (1) a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than 75% of the combined voting power of the voting securities of the Company or such surviving entity outstanding immediately after such merger or consolidation or (2) a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction in which no "person" (with the exceptions specified in clause (A) of this definition) acquires 25% or more of the combined voting power of the Company's then outstanding securities; or

(D) the stockholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets.

For purposes of paragraph 16 of this Plan, a "Change in Control of the Company" shall also be deemed to have occurred if the Company consummates a merger, consolidation, stock dividend, stock split or combination, extraordinary cash dividend, exchange offer, issuer tender offer or other transaction effecting a recapitalization of the Company (or similar transaction) (the "Transaction") and, in connection with the Transaction, a Designated Downgrading occurs with respect to the unsecured general obligations of the Company (the "Securities"), as described below:

(i) If the rating of the Securities by both Rating Agencies (defined hereinafter) on the date 60 days prior to the public announcement of the Transaction (a "Base Date") is equal to or higher than BBB Minus (as hereinafter defined), then a "Designated Downgrading" means that the rating of the Securities by either Rating Agency on the effective date of the Transaction (or, if later, the earliest date on which the rating shall reflect the effect of the Transaction) (as applicable, the "Transaction Date") is equal to or lower than BB Plus (as hereinafter defined); if the rating of the Securities by either Rating Agency on a Base Date is lower than BBB Minus, then a "Designated Downgrading" means that the rating of the Securities by either Rating Agency on the Transaction Date has decreased from the rating by such Rating Agency on the Base Date. In determining whether the rating of the Securities has decreased, a decrease of one gradation (+ and - for S&P and 1, 2 and 3 for Moody's, or the equivalent thereof by any substitute rating agency referred to below) shall be taken into account;

(ii) "Rating Agency" means either Standard & Poor's Corporation or its successor ("S&P") or Moody's Investors Service, Inc. or its successor ("Moody's");

(iii) "BBB Minus" means, with respect to ratings by S&P, a rating of BBB and, with respect to ratings by Moody's, a rating of Baa3, or the equivalent thereof by any substitute agency referred to below; and

(iv) "BB Plus" means, with respect to ratings by S&P, a rating of BB+ and, with respect to ratings by Moody's, a rating of BBB3, or the equivalent thereof by any substitute agency referred to below.

(v) The Company shall take all reasonable action necessary to enable each of the Rating Agencies to provide a rating for the Securities, but, if either or both of the Rating Agencies shall not make such a rating available, a nationally-recognized investment banking firm shall select a nationally-recognized securities rating agency or two nationally-recognized securities rating agencies to act as substitute rating agency or substitute rating agencies, as the case may be.

14 PRO-RATA PAYMENT FOLLOWING CHANGE IN CONTROL

Notwithstanding any of the preceding provisions of this Plan, upon the occurrence of any Change in Control of the Company, it shall be deemed, solely for purposes of this Plan, that each Participant's employment has terminated on the date of such Change in Control by reason of retirement and that each Award Cycle which was in progress on such date had begun at least 12 months before such date. Each Participant shall thereupon be paid a pro-rata portion of any pending Target Incentive Awards, in accordance with paragraph 9 hereof; provided,

however, that payment shall be calculated as if it were being paid solely in shares of Company common stock in accordance with paragraph 7 (C), and then actually shall be paid in cash with such shares valued at the higher of (i) the closing price of such shares as reported on the New York Stock Exchange - Composite Transactions on the date preceding and nearest the date the Change in Control occurred or (ii) the highest per share price for the common stock of the Corporation actually paid in connection with such Change in Control, provided, however, that such value shall not exceed the amount necessary to provide a fully equitable payment of such account, taking into consideration any adjustments made pursuant to paragraph 8 (D) (v) of the Plan with respect to any events or transactions constituting a Change in Control of the Company, or a part thereof.

15. PAYMENT OF PREVIOUSLY UNPAID AMOUNTS FOLLOWING CHANGE IN CONTROL

Notwithstanding any of the preceding provisions of this Plan, upon the occurrence of any Change in Control of the Company, if any Target Incentive Award amount which any Participant earned under this Plan during any Award Cycle which ended prior to the Change in Control has neither been paid to such Participant nor credited to such Participant's account under paragraph 8 hereof, such Target Incentive Award amount shall be paid to such Participant immediately following the first date on which such Target Incentive Award can be calculated and shall in no event be paid later than the later of (i) the first business day of April following the final year of the Award Cycle with respect to which such Target Incentive Award was earned, or (ii) the fifteenth (15th) day following the Change in Control.

16. PAYMENT OF DEFERRED ACCOUNT FOLLOWING A CHANGE IN CONTROL

Notwithstanding any of the preceding provisions of this Plan, as soon as possible following any Change in Control of the Company, payment shall be made, in cash, of the entire account of each Participant under paragraph 8 hereof. For purposes of calculating the amount of such payment, any shares of the Company's common stock credited to, or accrued in, any Participant's account shall be valued at the higher of (i) the closing price of such shares as reported on the New York Stock Exchange - Composite Transactions on the date preceding and nearest the date the Change in Control occurred or (ii) the highest per share price for the common stock of the Company actually paid in connection with such Change in Control; provided, however, that such value shall not exceed the amount necessary to provide a fully equitable payment of such account, taking into consideration any adjustments made pursuant to paragraph 8 (D) (v) of the Plan with respect to any events or transactions constituting a Change in Control of the Company, or a part thereof.

AMENDED AND RESTATED OCTOBER 23, 1996 AND MAY 19, 1997
EFFECTIVE JANUARY 1, 1997

SUPPLEMENTAL RETIREMENT AND SAVINGS PLAN
FOR SALARIED EMPLOYEES OF THE STANLEY WORKS

BACKGROUND. A. The Stanley Works (together with its wholly-owned U.S. subsidiaries, "Stanley") maintains certain retirement plans for its salaried employees that are designed to meet the requirements of Section 401(a) of the Internal Revenue Code (the "Code").

B. The benefits and contributions that may be provided under such retirement plans are limited on account of Sections 401 and 415 of the Code and certain other provisions of the Code.

C. Stanley maintains this Plan for Salaried Employees of The Stanley Works (the "Supplemental Plan") to provide certain employees with benefits that may not be provided under these retirement plans.

D. Stanley now desires to restate the Supplemental Plan.

TERMS OF THE SUPPLEMENTAL PLAN

1. EFFECTIVE DATE. This amendment and restatement shall be effective January 1, 1997.

2. DEFINITIONS. The following terms have the meanings set forth below.

"APPLICABLE LIMITATION" means each of:

(a) the limitation under Sections 401(a)(30) and 402(g)(1) of the Code on the amount of pre-tax elective contributions that may be made by an employee under the Savings Plan;

(b) the limitation in Section 401(a)(17) of the Code on the amount of compensation of an employee that may be taken into account under the Retirement Plan or Savings Plan;

(c) the limitation under the Savings Plan on the amount of an employee's pre-tax elective contributions or Stanley matching contributions imposed under the nondiscrimination rules of Section 401 of the Code;

(d) the exclusion from the "Compensation" utilized under the Retirement Plan of earnings deferred at the election of an employee pursuant to the Deferred Compensation Plan for Participants in Stanley's Management Incentive Plans; and

(e) the limitations in Section 415 of the Code on the maximum contributions that may be made under the Savings Plan and the maximum benefits that may be provided under the Retirement Plan.

"COMMITTEE" means the Finance and Pension Committee of the Board of Directors of The Stanley Works.

"ELIGIBLE EMPLOYEE" means a Highly Compensated Employee who is a participant in Stanley's Management Incentive Plans.

"401(K) DOLLAR LIMITS" means the dollar limitation described in paragraph (a) of the definition of Applicable Limitation.

"HIGHLY COMPENSATED EMPLOYEE" means a salaried employee of Stanley who during the applicable Plan Year is a highly compensated employee, as defined in Section 414(q) of the Code (i.e., W2 income, including contributions to health and dental plans, to flexible spending plans, and to the Savings Plan, exceeding the indexed amount [\$80,000 for 1997]).

"PLAN YEAR" means the plan year of a Qualified Plan.

"QUALIFIED PLAN" means each of the Savings Plan and the Retirement Plan.

"RETIREMENT PLAN" means The Stanley Works Retirement Plan.

"SAVINGS PLAN" means The Stanley Works 401(k) Savings Plan.

"SUPPLEMENTAL COMPANY CONTRIBUTION ACCOUNT" means the bookkeeping record that reflects amounts credited under Section 4.2.

"SUPPLEMENTAL EMPLOYEE CONTRIBUTION ACCOUNT" means the bookkeeping record that reflects amounts credited under Section 4.1.

"UNRESTRICTED QUALIFIED PLAN BENEFIT" means the benefit amount that would be payable to an individual under the Retirement Plan but for an Applicable Limitation.

3. PARTICIPATION IN THE SUPPLEMENTAL PLAN. 3.1. ELIGIBLE EMPLOYEE PARTICIPATION. Each Eligible Employee shall become a participant in the Supplemental Plan on the date as of which an amount is first credited on his or her behalf under Section 4.

3.2. REMAINING A PARTICIPANT. Subject to Section 7, an Eligible Employee shall remain a participant until all amounts to which he or she is entitled have been distributed.

4. CREDITING OF BENEFITS; ELECTIONS TO DEFER. 4.1. SUPPLEMENTAL EMPLOYEE

CONTRIBUTIONS. (a) EMPLOYEE CONTRIBUTIONS EXCEEDING 401(K) DOLLAR LIMITS. If an Eligible Employee's pre-tax elective contributions under the Savings Plan for a Plan Year are limited by the 401(k) Dollar Limits, the Eligible Employee may elect to defer a portion of compensation. The amount deferred for a Plan Year under this Section 4.1(a), when added to the pre-tax elective contributions for the Plan Year under the Savings Plan, shall not exceed 15% of compensation.

(b) EMPLOYEE CONTRIBUTIONS EXCEEDING OTHER LIMITS. If an Eligible Employee may not make pre-tax elective contributions under the Savings Plan for a Plan Year as a result of an Applicable Limitation (other than as described in Section 4.1(a)), the Eligible Employee may elect to defer a portion of compensation, up to the amount of such pre-tax elective contributions that could not be made.

(c) CREDITING OF EMPLOYEE CONTRIBUTIONS. Any amount deferred under this Section 4.1 shall be credited to a Supplemental Employee Contribution Account.

4.2. SUPPLEMENTAL COMPANY CONTRIBUTIONS. (a) MATCHING CONTRIBUTIONS FOR EMPLOYEE CONTRIBUTIONS EXCEEDING DOLLAR LIMITS. If an amount is credited to a Supplemental Employee Contribution Account under Section 4.1, there shall also be an amount credited to a Supplemental Company Contribution Account. This amount shall equal the contribution that would have been made by Stanley under the Savings Plan with respect to the amount credited under Section 4.1 if such amount had been contributed to the Savings Plan.

(b) MATCHING CONTRIBUTIONS AFFECTED BY OTHER LIMITS. If a Stanley contribution could not be made under the Savings Plan as a result of an Applicable Limitation (other than as described in Section 4.2(a)), an amount equal to such Stanley contribution that could not be made shall be credited to a Supplemental Company Contribution Account.

4.3. SUPPLEMENTAL RETIREMENT PLAN BENEFITS. If an Eligible Employee's Unrestricted Qualified Plan Benefit exceeds the benefit payable under the Retirement Plan, the excess amount, to the extent vested under Section 5.1, shall be provided under this Supplemental Plan.

4.4. CREDITING OF EARNINGS. A participant's Supplemental Employee Contribution Account and Supplemental Company Contribution Account shall be credited with the rate of return such accounts would have earned if they had been invested under the Savings Plan. In addition, these accounts shall be credited with any additional amount that would have been payable under the Retirement Plan to reflect IPA benefits. For purposes of crediting the rate of return, an amount shall be considered to be credited under Section 4.1 or 4.2 on the date on which it would have been allocated under the Savings Plan but for an Applicable Limitation.

4.5. PROCEDURES FOR ELECTING EMPLOYEE CONTRIBUTIONS. An election to defer compensation under Section 4.1 shall be made, and may be revoked, under rules established by the Committee. Any election to defer compensation shall be effective only as to compensation earned after the date of the election.

5. VESTING SCHEDULE. A participant's vested interest in a benefit provided under this Plan shall be determined in accordance with the vesting provisions of the particular Qualified Plan with respect to which the benefit is determined.

6. DISTRIBUTIONS. 6.1. TIME FOR PAYING BENEFITS. Amounts credited to a participant's Supplemental Employee Contribution Account or Supplemental Company Contribution Account shall be distributed upon retirement, death, disability or earlier separation from service with Stanley unless either the rules of Section 7.3 apply or the participant elects to have payments made on a later date specified in an election made under Section 6.3. Amounts payable under Section 4.3 (relating to Supplemental Retirement Plan Benefits) shall be distributed when benefit payments commence under the Retirement Plan.

6.2. FORM OF PAYMENT. Benefits attributable to an individual's Supplemental Employee Contribution Account and Supplemental Company Contribution Account shall be distributed in a cash lump sum payment. The benefit determined under Section 4.3 (relating to Supplemental Retirement Plan Benefits) shall be paid in a life annuity unless the participant elects a lump sum payment under Section 6.3.

6.3. ELECTIONS BY PARTICIPANTS. An election to receive a lump sum payment of the benefit payable under Section 4.3 (relating to Supplemental Retirement Plan Benefits) or to defer distributions of the Supplemental Employee Contribution and Supplemental Company Contribution Accounts may be made by a participant in writing prior to the beginning of the one year period that ends on the date on which the participant dies, becomes disabled, or otherwise separates from service. An election may be made after the beginning of such one year period only with the approval of the Committee.

6.4. ADJUSTMENTS TO DISTRIBUTIONS. Upon determining that a participant is indebted to Stanley, the Committee shall be entitled to offset such indebtedness, including any interest accruing thereon, against any payment that would otherwise be made on behalf of the participant.

6.5. DEATH BENEFICIARY. Upon a participant's death, any benefit payment shall be made to the beneficiary determined under the Qualified Plan to which the benefit relates unless the participant designated in writing a different beneficiary to receive such benefit. The benefit shall be paid in the manner provided in Section 6.2.

6.6. WITHHOLDING. To the extent required by law, Stanley shall withhold taxes from any payment due under the Plan.

7. INELIGIBILITY FOR COVERAGE. 7.1. BECOMING INELIGIBLE. Amounts shall not be credited under Section 4.1 or 4.2 upon either (a) a participant ceasing to be an Eligible Employee or (b) the Committee, in its sole discretion, determining that an Eligible Employee may no longer actively participate in the Plan.

7.2. RESUMING PARTICIPATION. An individual described in Section 7.1(a) shall resume

active participation in the Supplemental Plan upon again becoming an Eligible Employee. An individual described in Section 7.1(b) may again become an active participant at the discretion of the Committee. Once an individual resumes participation in the Supplemental Plan, amounts shall again be credited under Section 4.1 upon the filing of an election pursuant to Section 4.5, and amounts may also be credited under Section 4.2.

7.3. DISTRIBUTIONS TO INELIGIBLE INDIVIDUALS. An amount credited under Section 4 on behalf of an individual for a Plan Year in which such individual was not an Eligible Employee shall be distributed in a cash lump sum payment upon the earliest of the following: (a) death, (b) disability, (c) other separation from service with Stanley, or (d) the first day of the calendar year in which the individual attains age 60. No additional amount shall be credited to an account established in the name of an individual described in this subsection unless such individual becomes an Eligible Employee. If the individual becomes an Eligible Employee, amounts credited to an account established in the name of the individual while an Eligible Employee shall be distributed in accordance with Section 6, and other amounts shall be distributed in the manner described above in this subsection.

8. MISCELLANEOUS. 8.1. AMENDMENT OR TERMINATION. The Committee may at any time amend or terminate the Supplemental Plan without the consent of any participant or beneficiary.

8.2. ADMINISTRATION OF THE SUPPLEMENTAL PLAN. The Supplemental Plan shall be administered by the Committee. The Committee shall have the discretionary authority to interpret the Supplemental Plan and to make all determinations regarding eligibility for coverage and the benefits to be paid. Any denial by the Committee of a claim for benefits under the Supplemental Plan shall be stated in writing by the Committee and delivered or mailed to the appropriate individual. Such notice shall set forth the specific reasons for the denial. The Committee shall afford to any participant or beneficiary whose claim for benefits has been denied a reasonable opportunity for a review of the denial of the claim.

8.3. GOVERNING TEXT. The Supplemental Plan, including any amendments, shall constitute the entire agreement between Stanley and any employee, participant or beneficiary regarding the subject matter of the Supplemental Plan. The Supplemental Plan, including any amendments, shall be binding on Stanley, employees, participants, beneficiaries, and their respective heirs, administrators, trustees, successors and assigns.

8.4. ENFORCEABILITY OF PLAN PROVISIONS. If any provision of the Supplemental Plan shall, to any extent, be invalid or unenforceable, the remainder of the Supplemental Plan shall not be affected, and each other provision of the Supplemental Plan shall be valid and enforced to the fullest extent permitted by law.

8.5. RIGHTS OF PARTICIPANT. Any person entitled to receive benefits under the Supplemental Plan shall have the rights of an unsecured general creditor of Stanley.

8.6. CLAIMS OF CREDITORS. The right of any participant or beneficiary to a benefit under

the Supplemental Plan shall not be subject to attachment or other legal process for the debts of such participant or beneficiary. Except as provided in Section 6.4, a benefit of a participant or beneficiary shall not be subject to anticipation, alienation, sale, transfer, assignment or encumbrance.

8.7. SPECIAL DISTRIBUTIONS. Whenever, in the opinion of the Committee, a person entitled to receive a benefit under the Plan is unable to manage his or her financial affairs, the Committee may direct that payment be made to a legal representative or relative of such person for his or her benefit. Alternatively, the Committee may direct that any payment be applied for the benefit of such person in such manner as the Committee considers advisable. Any payment made in accordance with this Section shall be a complete discharge of any liability for the making of such payment under the provisions of the Supplemental Plan.

8.8. TERMS OF EMPLOYMENT. Participation in the Supplemental Plan shall not give an individual any right to remain in the service of Stanley, and an individual shall remain subject to discharge to the same extent as if the Supplemental Plan had not been adopted.

Effective--May 20, 1997

THE STANLEY WORKS

SUPPLEMENTAL EXECUTIVE RETIREMENT PROGRAM

The Supplemental Executive Retirement Program ("SERP") provides a supplemental retirement benefit to its Participants. As explained below, this supplemental benefit is a supplement to the defined benefit under Stanley's pension plans.

1. TARGET BENEFIT. The "Target Benefit" for a Participant, expressed as a life annuity equal to a percentage of Average Pay and subject to discount and to certain Offsets, will be based on years of service according to the following schedule.

- 3% for each of the first 5 years
- 2% for each of the next 15 years
- 1% for each of the 5 years thereafter

For example, upon a Participant's retiring at age 60 after 20 years of service, the Participant's Target Benefit would be 45% of Average Pay.

2. TERMINATION PRIOR TO AGE 60.

(a) TERMINATION BEFORE AGE 54. No SERP benefit will be paid to any Participant whose employment terminates before the age of 54.

(b) DISCOUNT FOR RETIREMENT PRIOR TO AGE 60. For each month prior to age 60 that the Participant retires, the Target Benefit will be reduced .167% (i.e., 2% per year). For example, a Participant who retires at age 55 after 20 years of service would have a benefit, before Offsets, equal to 90% of the Target Benefit, or 40.5% ($45\% \times 90\% = 40.5\%$) of Average Pay.

3. OFFSETS. The benefit otherwise payable under the SERP as explained in sections 1 and 2 will be reduced by the "Offsets" described in sections 3(a) and 3(b)

(a) the benefit under Stanley's pension plan including pension benefits restored by Stanley's excess benefit plan; and

(b) the Participant's Social Security benefit;¹

resulting in the benefit net of Offsets.

4. PARTICIPANTS. The Participants (the "Participants") in the SERP will be Stanley's chief executive officer and such other executives not to exceed 24 as shall be designated by the chief executive officer and whose names shall be filed with the records of the Compensation and Organization Committee (the "Committee") of Stanley's Board.

5. TIME FOR PAYING BENEFITS; FORM OF PAYMENT. Amounts payable under the SERP will be distributed when benefit payments commence under Stanley's pension plan. The form of payment of benefits under the SERP will be a life annuity unless a timely election is made to receive a lump sum, in which case the form of payment will be a lump sum computed in the same manner as under the Stanley pension plan. To be timely, an election to receive a lump sum payment must be made in writing prior to the beginning of the one-year period preceding the date on which the Participant dies, becomes disabled, or otherwise separates from service; an election made after the beginning of such one-year period will be considered timely only with the approval of the Committee.

6. AVERAGE PAY. Average pay will be one-third of the Participant's highest total pay (salary and management incentive) as measured for purposes of Stanley's pension plan (including the restoration of pension benefits by Stanley's excess benefit plan) for any consecutive 36-month period.

7. DEATH BENEFICIARY. Upon a Participant's death, any benefit payment will be made to the beneficiary determined under Stanley's qualified pension plan unless the Participant designated in writing a different beneficiary to receive such benefit.

8. MISCELLANEOUS.

(a) AMENDMENT. The Committee may at any time amend the SERP so long as the benefits of no one then a Participant are diminished as a result.

1 If the Participant retires prior to being eligible for Social Security, the Social Security benefit offset will not commence until the Participant is eligible for Social Security. For example, for a retirement in 1997 by a Participant who is 60 years old, there would be no Social Security offset until the Participant is 62, the age of eligibility for Social Security.

(b) ADMINISTRATION OF THE SERP. The SERP will be administered by the Committee. The Committee is vested with full authority (including full discretionary authority) to administer, interpret, and make rules regarding the SERP as it may deem advisable and to make determinations in its discretion that shall be final, binding, and conclusive upon all persons. No member of the Board of Directors or the Committee will be liable for any action or determination made in good faith with respect to the SERP.

(c) GOVERNING TEXT. The SERP, including any amendments, will constitute the entire agreement between Stanley and any Participant or beneficiary regarding the subject matter of the SERP. The SERP, including any amendments, will be binding on Stanley, Participants, beneficiaries, and their respective heirs, administrators, trustees, successors, and assigns.

(d) RIGHTS OF PARTICIPANT. Any person entitled to receive benefits under the SERP will have the rights of an unsecured general creditor of Stanley.

(e) CLAIMS OF CREDITORS. The right of any Participant or beneficiary to a benefit under the SERP will not be subject to attachment or other legal process for the debts of such Participant or beneficiary. A benefit of a Participant or beneficiary will not be subject to anticipation, alienation, sale, transfer, assignment, or encumbrance.

(f) SPECIAL DISTRIBUTIONS. Whenever, in the opinion of the Committee, a person entitled to receive a benefit under the SERP is unable to manage his or her financial affairs, the Committee may direct that payment be made to a legal representative or relative of such person for his or her benefit. Alternatively, the Committee may direct that any payment be applied for the benefit of such person in such manner as the Committee considers advisable. Any payment made in accordance with this section will be a complete discharge of any liability for the making of such payment under the provisions of the SERP.

(g) TERMS OF EMPLOYMENT. Participation in the SERP will not give an individual any right to remain in the service of Stanley, and an individual will remain subject to discharge to the same extent as if the SERP had not been adopted.

September 17, 1997

John M. Trani
Chairman and Chief Executive Officer
The Stanley Works
1000 Stanley Drive
New Britain, CT 06053

Dear John:

You, along with 12 other Stanley executives, are covered under Stanley's Supplemental Executive Retirement Program ("SERP"). Generally, the SERP provides a benefit (in combination with Stanley's other pension plans) of 45% of average pay at age 60 after 20 years of service.

Regrettably, there is a shortfall between this Stanley SERP benefit and the pension benefit you would have received from your former employer if,

- (a) on or after your 60th birthday, you had retired from your former employer, or
- (b) prior to your 60th birthday, your employment with your former employer had terminated at the request of your former employer.

Stanley's Board wishes to make you whole with respect to such shortfall in pension benefit. Consequently Stanley agrees with you as follows:

1. If
 - (a) your Stanley employment terminates prior to March 15, 2005(1) (other than as a result of death), and

- - - - -
(1) Your 60th birthday.

(b) such termination is at the request of the Board (but is not for "cause"(2)) or is because of your illness or disability,

then Stanley will(3) "top up" the SERP benefit so that, in combination with Stanley's other pension plans, you will receive a benefit not less than the product of

(i) your Average Pay (as defined in the SERP(4)), times

(ii) the number of 12-month periods (and fractions thereof) that have elapsed from October 1, 1978(5) to the later of your last day worked (and any following vacation period) and any period during which severance is paid, times

(iii) 1.75%(6);

such benefit to be paid until March 15, 2005. After March 15, 2005, Stanley will "top up" the SERP benefit so that, in combination with Stanley's other pension plans, you will receive a benefit not less than the product of 46.375%(7) times your Average Pay, reduced by \$83,280(8).

2. If your Stanley employment terminates on or after March 15, 2005 (other than as a

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(2) Using the following definition of "cause" from your Employment Agreement: "if (1) the Executive is convicted of a felony, including the entry of a guilty or nolo contendere plea, or (2) the Executive engages in conduct that constitutes willful gross neglect or willful gross misconduct in carrying out his duties, resulting, in either case, in material harm to the Company, monetarily or otherwise, unless the Executive reasonably believed in good faith that such act or non-act was in (or not opposed to) the best interests of the Company."

(3) Stanley may, at the discretion of the Board, "top up" the SERP as described, even if the conditions of this clause (b) are not met.

(4) "Average pay will be one-third of the Participant's highest total pay (salary and management incentive) as measured for purposes of Stanley's pension plan (including the restoration of pension benefits by Stanley's excess benefit plan) for any consecutive 36-month period."

(5) Your date of hire with your former employer.

(6) The 12-month percentage multiplier used in your former employer's serp.

(7) 1.75% times 26.5 (the number of 12-month periods that would have elapsed from October 1, 1978, your date of hire by your former employer, to March 15, 2005, your 60th birthday).

(8) The pension benefit to be paid to you by your former employer commencing March 15, 2005.

result of death), then Stanley will "top up" the SERP benefit so that, in combination with Stanley's other pension plans, you will receive a benefit not less than the product of 46.375% times your Average Pay, reduced by \$83,280.

THE STANLEY WORKS

/s/ Stillman B. Brown

Stillman B. Brown, Chairman
Compensation and Organization Committee

Adopted--September 28, 1994
Amended--March 1, 1995
Approved by shareholders--April 19, 1995
Amended--December 18, 1996

THE STANLEY WORKS
STOCK OPTION PLAN
FOR NON-EMPLOYEE DIRECTORS

1. PURPOSE.

The purpose of The Stanley Works Stock Option Plan for Non-Employee Directors (the "Plan") is to promote the interests of The Stanley Works (the "Company") and its shareholders by encouraging Non-Employee Directors of the Company to have a direct and personal stake in the performance of the Company's Common Stock.

2. DEFINITIONS.

Unless the context clearly indicates otherwise, the following terms have the meanings set forth below. Whenever applicable, the masculine pronoun shall include the feminine pronoun and the singular shall include the plural.

"Biennial Option" or "Biennial Option Grant" means an Option granted to a Non-Employee Director in accordance with Section 7(a)(i) of the Plan.

"Board of Directors" or "Board" means the Board of Directors of the Company.

"Business Day" shall mean any day except Saturday, Sunday or a legal holiday in the State of Connecticut.

"Code" means the Internal Revenue Code of 1986, as amended, now in effect or as amended from time to time and any successor provisions thereto.

"Common Stock" means the common stock, par value \$2.50 per share, of the Company.

"Fair Market Value" of a share of Common Stock on any particular date means the mean average of the high and the low price of a share of the Common Stock as quoted on the New York Stock Exchange Composite Tape on the date as of which fair market value is to be determined or, if there is

no trading of Common Stock on such date, such mean average of the high and the low price on the next preceding date on which there was such trading.

"Grant Date", as used with respect to a particular Option, means the date on which such Option is granted pursuant to Section 7(a) of the Plan.

"Grantee" means the Non-Employee Director to whom an Option is granted pursuant to the Plan.

"Immediate Family Members" shall mean the spouse, children and grandchildren of a Grantee.

"Initial Option" or "Initial Option Grant" means the Option granted to a Non-Employee Director who is first elected or appointed to the Board after September 30, 1994 and prior to December 18, 1996 in accordance with Section 7(a)(ii) of the Plan.

"Option" means an Initial Option or Biennial Option granted pursuant to the Plan to purchase shares of Common Stock which shall be a non-qualified stock option not intended to qualify as an incentive stock option under Section 422 of the Code.

"Non-Employee Director" shall mean a member of the Board of Directors who is not an employee of the Company or any Subsidiary.

"Plan" means The Stanley Works Stock Option Plan for Non-Employee Directors as set forth herein and as amended from time to time.

"Retirement", as applied to a Non-Employee Director, shall mean when such director ceases to serve as a member of the Board following attaining sixty (60) years of age and having served as a member of the Board for a period of at least sixty months.

"Subsidiary" shall mean a "subsidiary corporation" of the Company as defined in Section 425(f) of the Code.

"1934 Act" means the Securities Exchange Act of 1934, as amended, now in effect or as amended from time to time and any successor provisions thereto.

3. ADMINISTRATION.

The Plan shall be administered by the Board, which shall have full power and authority, subject to the provisions of the Plan, to supervise administration of the Plan and interpret the provisions of the Plan and any Options granted hereunder. Any decision by the Board shall be final and binding on all parties.

No member of the Board shall be liable for any determination, decision or action made in good faith with respect to the Plan or any Option under the Plan.

4. ELIGIBILITY.

The persons eligible to receive Options under the Plan are the Non-Employee Directors.

5. EFFECTIVE DATE AND TERM OF THE PLAN.

The Plan shall become effective upon its adoption by the Board of Directors, provided, that no Option granted pursuant to the Plan will vest or shall be exercised prior to the approval of the Plan by the Company's shareholders within twelve (12) months of its adoption by the Board. Unless previously terminated by the Board, the term during which awards may be granted under the Plan shall expire on the tenth anniversary of the adoption of the Plan by the Board of Directors.

6. SHARES SUBJECT TO THE PLAN.

The shares of Common Stock that may be delivered upon the exercise of Options under the Plan shall be shares of the Company's authorized Common Stock and may be unissued shares or reacquired shares, as the Board of Directors may from time to time determine. Subject to adjustment as provided in Section 13 hereof, the aggregate number of shares to be delivered under the Plan shall not exceed 200,000 shares. If any shares are subject to an Option which for any reason expires or terminates during the term of the Plan prior to the issuance of such shares, the shares subject to but not delivered under such Option shall be available for issuance under the Plan. If, on any Grant Date, the aggregate number of shares of Common Stock subject to Option grants on that date exceeds the remaining number of shares reserved for issuance under the Plan, the number of Option shares awarded to each Non-Employee Director to whom an Option shall be granted on such date shall be reduced pro rata so that the aggregate number of Option shares awarded to such Non-Employee Directors equals the number of reserved shares of Common Stock remaining under the Plan.

7. OPTIONS.

(a) Grant of Options.

(i) The 1994 and 1996 Option Grants. On September 30, 1994 and August 1, 1996, each Non-Employee Director on that date shall automatically be granted an Option, upon the terms and conditions specified in the Plan, to purchase 1,000 shares of Common Stock.

(ii) Initial Option Grants to Newly-Elected Non-Employee Directors. Any person who is elected as a Non-Employee Director for the first time after September 30, 1994 and prior to December 18, 1996 shall automatically be granted an Initial Option, upon the terms and conditions specified in the Plan, immediately following the first Annual Meeting of the Company's Shareholders at which such person is first elected a Non-Employee Director by the Shareholders. The number of shares of Common Stock subject to such Initial Option shall equal the number of shares of Common Stock such Non-Employee Director would have received under option grants under the Plan if such Non-Employee Director had been a Non-Employee Director at all times between September 1, 1994 and the date of such person's election as a Non-Employee Director.

(iii) Discretionary Option Grants. On and after December 18, 1996, Non-Employee Directors may be granted Options, upon the terms and conditions specified in the Plan, to purchase shares of Common Stock in amounts as may be determined by the Board of Directors.

(b) Terms of Options. Each Option granted under the Plan shall have the following terms and conditions:

- (i) Price. The exercise price per share of each Option shall equal the greater of one hundred percent (100%) of the Fair Market Value of a share of Common Stock on the Grant Date or the par value per share of the Common Stock on the date of exercise of such option.
- (ii) Term. The term of each Option shall be for a period of ten (10) years from the Grant Date unless terminated earlier in accordance with Section 12 of the Plan.
- (iii) Time of Vesting and Exercise. An Option shall vest and become nonforfeitable when, and only if, the Grantee continues to serve as a Non-Employee Director for a period of six (6) months following the Grant Date of such Option. Unless the time of its exercisability is accelerated in accordance with the Plan, each Option that has vested shall be exercisable in full on or after the first anniversary of its Grant Date.
- (iv) Acceleration of Exercisability. Notwithstanding the provisions of subparagraph (iii) hereof, an Option that has vested shall become fully exercisable upon the occurrence of the Grantee's death or withdrawal from the Board of Directors by reason of such Non-Employee Director's Retirement.

- (v) Option Agreement. Each Option shall be evidenced by an Option Agreement substantially in the form attached to this Plan as Appendix A.

8. EXERCISE OF OPTIONS.

(a) Each Option granted shall be exercisable in whole or in part at any time, or from time to time, during the Option term as specified in the Plan, provided that the election to exercise an Option shall be made in accordance with applicable Federal laws and regulations. Each Option may be exercised by delivery of a written notice to the Company stating the number of shares to be exercised and accompanied by the payment of the Option exercise price therefor in accordance with this Section. The Grantee shall furnish the Company, prior to the delivery of any shares upon the exercise of an Option, with such other documents and representations as the Company may require, to assure compliance with applicable laws and regulations.

(b) No Option may at any time be exercised with respect to a fractional share. In the event that shares are issued pursuant to the exercise of an Option, no fractional shares shall be issued and cash equal to the Fair Market Value of such fractional share on the date of the delivery of the exercise notice shall be given in lieu of such fractional shares.

(c) No shares shall be delivered pursuant to the exercise of any Option, in whole or in part, until qualified for delivery under such securities laws and regulations as the Committee may deem to be applicable thereto and until payment in full of the Option price is received by the Company in cash, by check or in shares of Common Stock as provided in Section 9 hereof. Neither the holder of an Option nor such holder's transferee, legal representative, legatee, or distributee shall be or be deemed to be a holder of any shares subject to such Option unless and until a certificate or certificates therefor is issued in his or her name or a person designated by him or her.

9. STOCK AS FORM OF EXERCISE PAYMENT.

A Grantee who owns shares of Common Stock may elect to use the previously acquired shares, valued at the Fair Market Value on the last Business Day preceding the date of delivery of such shares, to pay all or part of the exercise price of an Option, provided, however, that such form of payment shall not be permitted unless at least one hundred shares of such previously acquired shares are required and delivered for such purpose and the shares delivered have been held by the Grantee for at least six months.

10. WITHHOLDING TAXES FOR AWARDS.

Each Grantee exercising an Option as a condition to such exercise shall pay to the Company the amount, if any, required to be withheld from distributions resulting from such exercise under applicable Federal and State income tax laws ("Withholding Taxes"). Such Withholding Taxes shall be payable as of the date income from the award is includable in the Grantee's gross income for Federal income tax purposes (the "Tax Date"). The Grantee may satisfy this requirement by remitting to the Company in cash or by check the amount of such Withholding Taxes or a number of previously owned shares of Common Stock having an aggregate Fair Market Value as of the last Business Day preceding the Tax Date equal to the amount of such Withholding Taxes. For the purposes of this Section 10, the exercise of an Option by a transferee of such Option pursuant to Section 11(b) hereof, shall be deemed to be an exercise of the Option by the Grantee.

11. TRANSFER OF AWARDS.

(a) Options granted under the Plan may not be transferred except (i) by will or the laws of descent and distribution (ii) pursuant to a qualified domestic relations order, as defined in the Code, or (iii) pursuant to the provisions of Subsection (b) below, and, except as provided in Subsection (b) below, during the Grantee's lifetime, may be exercised only by said Grantee or by said Grantee's guardian or legal representative.

(b) A Grantee may transfer all or a portion of the Options granted to the Grantee to (i) an Immediate Family Member or Immediate Family Members, (ii) a trust or trusts for the exclusive benefit of an Immediate Family Member or Immediate Family Members, or (iii) a partnership or partnerships in which an Immediate Family Member or Immediate Family Members is the only partner or are the only partners, provided that (y) there shall be no consideration for such transfer, and (z) subsequent transfers of transferred Options shall be prohibited except those in accordance with subsection (a) above. Following a transfer, any such transferred Options shall continue to be subject to the same terms and conditions as were applicable immediately prior to transfer, provided that for the purposes of Sections 9 and 15, hereof, the term "Grantee" shall be deemed to refer to the transferee. The events of termination of director status in Section 12 hereof shall continue to be applied with respect to the original Grantee, following which the Options shall be exercisable by the transferee only to the extent, and for the periods specified in Section 12. Neither the Board, the Company nor any agent, employee or representative thereof shall be under any duty under the Plan or otherwise to notify any transferee, pursuant to the terms of either subsection (a) above or this subsection (b), of any event which might have an impact on the value or exercisability of a transferred Option, including,

without limitation, early termination of the Option on account of termination of the original Grantee's director status.

12. TERMINATION OF DIRECTOR STATUS.

Upon the termination of a Grantee's service as a member of the Board of Directors for any reason other than death or Retirement, the Grantee may exercise an Option that has vested to the full extent of the number of the shares of Common Stock remaining under such Option, regardless of whether such Option was previously exercisable, until the earlier of the expiration of its original term or one year after the date of such termination. Upon the termination of Board membership of any such Grantee due to Retirement, the Grantee may purchase some or all of the shares covered by the Grantee's Options that have vested prior to such termination, regardless of whether such Option was previously exercisable, until the expiration of such Option's original term. Upon the death of any such Grantee while serving on the Board or of any retired Grantee, may exercise some or all of the Grantee's Options that have vested prior to such termination of Board membership, regardless of whether such Option was previously exercisable, until the expiration of such Option's original term.

13. CHANGES IN COMMON STOCK.

In the event of a merger, consolidation, reorganization, recapitalization, stock dividend, stock split, or other changes in corporate structure or capitalization affecting the Common Stock, such appropriate adjustment shall be made in the number, kind, option price, etc., of shares subject to Options granted under the Plan, including appropriate adjustment in the maximum number of shares referred to in Section 6 of the Plan, as may be determined by the Board.

14. LEGAL RESTRICTIONS.

The Company will not be obligated to issue shares of Common Stock or make any payment if counsel to the Company determines that such issuance or payment would violate any law or regulation of any governmental authority or any agreement between the Company and any national securities exchange on which the Common Stock is listed. In connection with any stock issuance or transfer, the person acquiring the shares shall, if requested by the Company, give assurances satisfactory to counsel to the Company regarding such matters as the Company may deem desirable to assure compliance with all legal requirements. The Company shall in no event be obliged to take any action in order to cause the exercise of any award under the Plan.

15. NO RIGHTS AS SHAREHOLDERS.

No Grantee and no beneficiary or other person claiming through a Grantee shall have any interest in any shares of Common Stock allocated for the purposes of the Plan or subject to any award until such shares of Common Stock shall have been transferred to the Grantee or such person. Furthermore, the existence of awards under the Plan shall not affect: the right or power of the Company or its stockholders to make adjustments, recapitalizations, reorganizations or other changes in the Company's capital structure; the dissolution or liquidation of the Company, or the sale or transfer of any part of its assets or business; or any other corporate act, whether of a similar character or otherwise.

16. BOARD MEMBERSHIP.

Nothing in the Plan or in any Option shall confer upon any Grantee any right to continue as a director of the Company or interfere in any way with the right of the Company's shareholders to remove a director at any time.

17. CHOICE OF LAW.

The validity, interpretation and administration of the Plan and of any rules, regulations, determinations or decisions made thereunder, and the rights of any and all persons having or claiming to have any interest therein or thereunder, shall be determined exclusively in accordance with the laws of the State of Connecticut.

18. AMENDMENT AND DISCONTINUANCE.

Subject to the limitation that the provisions of the Plan shall not be amended more than once every six months other than to comport with changes in the Code or regulations thereunder, the Board of Directors may alter, suspend, or discontinue the Plan, but may not, without the approval of a majority of the holders of the Common Stock, make any alteration or amendment thereof which operates (a) to increase the total number of shares which may be granted under the Plan, (b) to extend the term of the Plan or the option periods provided in the Plan, (c) to decrease the option price provided in the Plan, or otherwise materially increase the benefits accruing to Grantees through awards under the Plan, or (d) to modify the eligibility requirements for participation in the Plan.

STOCK OPTION AGREEMENT
UNDER
THE STANLEY WORKS STOCK OPTION PLAN
FOR NON-EMPLOYEE DIRECTORS

Pursuant to Section 7 of The Stanley Works Stock Option Plan for Non-Employee Directors (the "Plan"), The Stanley Works (the "Company"), this day of _____, 199____, hereby grants to ("Director") a non-qualified stock option to purchase an aggregate of [One Thousand (1,000) shares (in the case of a 1994 or 1996 Option)] [_____ shares (in the case of an Initial Option)] [_____ shares (in the case of a discretionary Option)] of the Common Stock of the Company at \$ _____ per share, on the terms and conditions hereinafter set forth and set forth in the Plan. This option will expire at the Company's close of business on _____, 19____, unless sooner terminated in accordance with the terms of the Plan.

1. The Company hereby grants to Director a non-qualified stock option (the "Option") to purchase on or before the expiration date indicated above, at the purchase price stated above, the number of shares of the Company's Common Stock set forth above. No option granted under the Plan shall be exercised or will vest unless and until the Plan is approved by the Company's shareholders.

2. The term of this Option shall commence on the date of this Agreement and shall terminate, unless sooner terminated by the terms of the Plan, at the close of business on the day preceding the tenth anniversary of the date of this Agreement as set forth above, if the Company is open for business on such day, or the close of the Company's business on the next preceding day that the Company is open for business. This Option shall vest and become nonforfeitable when, and only if, the Grantee continues to serve as a Non-Employee Director for a period of six (6) months following the Grant Date of this Option set forth above. No stock may be purchased hereunder until one year after the Grant Date of this Option set forth above. Thereafter, this Option may be exercised in whole or in part in accordance with the terms of the Plan during the term of the Option, unless sooner terminated by the terms of the Plan. This Option shall become immediately exercisable under the circumstances described in Section 7(b)(iv) of the Plan.

3. This Option may be exercised, in whole or in part, by written notification delivered in person or by mail to the Secretary of the Company at its world headquarters at 1000 Stanley Drive, New Britain, Connecticut. Such notification shall specify the number of shares with respect to which the Option is being exercised and shall be accompanied by payment for such shares. The Secretary of the Company will provide Director with a form of exercise notice upon request. The Option may not be exercised with respect to a fractional share. Payment is to be made by check payable to the order of the Company or by one of the alternative methods of payment described in the Plan. No shares shall be sold or delivered hereunder until full payment for such shares has been made and all checks delivered in payment therefor have been collected. Director shall not have any rights of a shareholder with respect to any Common Stock received upon exercise of the Option until certificates for such Common Stock have been actually issued to Director in accordance with the terms hereof.

4. The Company shall not be required to issue or deliver any certificate or certificates for shares of its Common Stock purchased upon the exercise of any part of this Option prior to (i) the admission of such shares to listing on any stock exchange on which the Common Stock may then be listed, (ii) the completion of any registration or other qualification of such shares under any applicable law, rule or regulation, (iii) the obtaining of any consent or approval or other clearance from any governmental agency which the Company determines to be necessary or advisable, and (iv) the payment to the Company, upon its demand, of any amount requested by the Company for the purpose of satisfying its liability, if any, to withhold federal, state or local income or earnings tax or any other applicable tax or assessment (plus interest or penalties thereon, if any, caused by a delay in making such payment) incurred by reason of the exercise of this Option or the transfer of such shares thereupon. The Option shall be exercised and shares of the Company's Common Stock issued only upon compliance with the Securities Act of 1933, as amended (the "Act"), and any other applicable securities laws, and Director agrees to comply with any requirements imposed by the Committee.

5. This Option is not transferrable by Director otherwise than (a) by will or by the laws of descent and distribution (b) pursuant to a qualified domestic relations order, as defined in the Code, or (c) pursuant to the immediately following sentence and is exercisable, except as provided in the immediately following sentence, during Director's life, only by Director or by Director's guardian or legal representative. The Director may transfer all or a portion of this Option to (i) an Immediate Family Member or Immediate Family Members, (ii) a trust or trusts for the exclusive benefit of such Immediate Family Member or Immediate Family Members, or (iii) a partnership or partnerships in which such Immediate Family Member or Immediate Family Members

is the only partner or are the only partners, all in accordance with and subject to the provisions of Section 11 of the Plan. Any attempted assignment, transfer, pledge, hypothecation or other disposition of the Option contrary to the provisions hereof shall be null and void. This Option does not confer upon Director any right with respect to continuation of Director's service as a director of the Company or any of its subsidiaries, and will not interfere in any way with the right of the Company's shareholders or the shareholders of any of its subsidiaries to terminate Director's service as a director.

6. Upon the termination of Director's service as a member of the Board of Directors, the Director or his or her transferee may exercise this Option, provided that it has vested, to the full extent of the number of the shares of Common Stock remaining under such Option, regardless of whether such Option was previously exercisable, in accordance with the conditions of Section 12 of the Plan.

7. This Option shall be irrevocable during the Option period and its validity and construction shall be governed by the laws of the State of Connecticut. The terms and conditions herein set forth are subject in all respects to the terms and conditions of the Plan, which shall be controlling. You agree to execute such other agreements, documents or assignments as may be necessary or desirable to effect the purposes of this Agreement.

8. The grant of this Option shall be binding and effective only if this Agreement is executed by or on behalf of the Company and by you and a signed copy is returned to the Company.

9. All capitalized terms used in this Agreement which are not defined herein shall have the meaning given to them in the Plan unless the context clearly requires otherwise.

THE STANLEY WORKS

By _____
Its

I hereby acknowledge receipt of the Stock Option (the "Option") granted on the date shown above, which has been issued

to me under the terms and conditions of The Stanley Works Stock Option Plan for Non-Employee Directors. I agree to conform to all of the terms and conditions of the Option and the Plan.

Date: _____ Your Signature: _____

April 30, 1996

Mr. Paul W. Russo
56 Pheasant Chase Road
West Hartford, CT 06117

Termination Protection Agreement and Related General Release

Dear Paul:

On April 17 I announced my plans for retirement as well as the Board's decision to commence an external search to find my replacement.

I recognize that your situation is different from that of others at Stanley with respect to job security inasmuch as you have been here at Stanley only a short while. Moreover it is always possible that the new CEO may (a) want to hire a person to head up strategic planning and development who is to the liking of the new CEO, or (b) the new CEO may change the strategic direction of Stanley (even though you accepted your position with Stanley based in part on your understanding of Stanley's current strategic direction).

In recognition of these issues summarized in clauses (a) and (b) above, Stanley is willing to provide you with certain financial protection as set forth in this Termination Protection Agreement in the event either of these situations occurs, in return for your making certain agreements as set forth below and in return for your signing and delivering to Stanley the Agreement and General Release attached as Exhibit A to this letter and your signing and delivering the letter attached as Exhibit B to this letter. Subject to the foregoing, you and Stanley agree as follows.

1. Termination on or before April 17, 2001. This Termination Protection Agreement covers any "termination" of which the "termination date" is on or before April 17, 2001.

2. "Termination" and "Termination Date". For purposes of this Termination

Protection Agreement your "termination" shall mean either of the following:

a. The actual termination of your employment by Stanley. In the case of your "termination" as described in this section 2a, your "termination date" will be the date your employment actually terminates.

b. Stanley substantially changes its strategic direction from the strategy summarized on pages 2-13 of Stanley's Annual Report for 1995, and you terminate your Stanley employment. In the case of your "termination" as described in this section 2b, your "termination date" will be the date your employment actually terminates. In the event Stanley disagrees with your opinion that Stanley's strategic direction has so changed it will promptly refer the matter to Stillman B. Brown (or if he is unable to act, to the member of Stanley's Board of Directors who is then chair of its Audit Committee) for final determination in his sole discretion as to whether or not Stanley's strategic direction has so changed.

3. Benefits Following Termination. Subject to the requirement that on or before the 30th day following your "termination" you shall have executed and delivered to Stanley the Agreement and General Release in the form of Exhibit A to this letter and that not less than 7 days thereafter you shall have signed and delivered to Stanley the letter in the form of Exhibit B to this letter, in the event of your "termination" your "benefits" will be continued until the first anniversary of your "termination date" (in the case of "termination" covered by section 2b, your benefits will be continued until the earlier of the first anniversary of your "termination date" or your having become gainfully employed). Your "benefits" will consist of the following.

a. Monthly payments equal to your base salary, less lawful deductions, as in effect at your "termination date". You agree that such payments will be deemed to include any entitlement you may have under Stanley's vacation and severance pay policies.

b. Coverage under the medical and dental plans in which you are enrolled on your "termination date", subject to your contributions as if you were an employee.

c. Coverage under Stanley's life and accidental death and dismemberment insurance in which you are enrolled on your "termination date", subject to your contributions as if you were an employee.

d. Coverage under Stanley's short-term and long-term disability plans in which you are enrolled on your "termination date", subject to your contributions as if you were an employee.

e. Use of the company-provided automobile, if any, which you are using immediately prior to your "termination date".

f. Participation in the Management Incentive Plan on a prorated basis.

g. For purposes of the Stock Option Plan you will be deemed to be an employee until such anniversary (in the case of "termination" covered by section 2b, until the earlier of the first anniversary of your "termination date" or your having become gainfully employed), whereupon your employment will be deemed to have terminated for purposes of the Stock Option Plan. You will receive no further stock option grants after your "termination".

h. Out placement services, if they are needed, through Drake, Beam, Morin until such anniversary.

i. For purposes of Stanley's pension and savings plans your employment will cease as of your "termination date".

j. Stanley will not contest your receipt of unemployment compensation benefits.

4. Notice to Stanley of Gainful Employment. You agree to promptly advise Stanley by faxed notice sent to Stanley's General Counsel at 860-827-3911 if, on or before the first anniversary of your "termination date", you become gainfully employed.

If you are in agreement with the foregoing, please sign and return a copy of this letter.

Sincerely yours,

Richard Ayers

Agreed:

Paul W. Russo

Paul W. Russo

Agreement and General Release

I, Paul W. Russo, as a condition to my receiving the "benefits" provided for in the Termination Protection Agreement (the "Termination Protection Agreement"), dated March 25, 1998, between The Stanley Works ("Stanley") and me, and in consideration therefor and for the performance of The Stanley Works thereunder, agree with The Stanley Works as follows (all defined terms used without definition have the meaning assigned to them in the Termination Protection Agreement).

1. I understand that I would not receive the benefits specified in sections 2a through 2j of the Termination Protection Agreement except for my execution of this Agreement and General Release and my fulfillment of the promises contained herein.

2. I understand that I may revoke this Agreement and General Release for a period of 7 business days following the day I execute this Agreement and General Release and this Agreement and General Release shall not become effective or enforceable until the revocation period has expired. Any revocation within this period must be submitted, in writing, to The Stanley Works, to the attention of its General Counsel and state, "I hereby revoke my acceptance of the Agreement and General Release." Such revocation must be personally delivered to such General Counsel or mailed by certified or express mail to such General Counsel at The Stanley Works, and postmarked within seven 7 business days of execution of this Agreement and General Release.

3. I, of my own free will, knowingly and voluntarily release and forever discharge Stanley, of and from any and all actions or causes of action, suits, claims, charges, complaints, contracts (whether oral or written, express or implied from any source), and promises, whatsoever, in law or equity, which, against Stanley, I, my heirs, executors, administrators, successors, and assigns (referred to collectively throughout this Agreement as "PWR") ever had, now have, may now have or hereafter can, shall or may have, as of my "termination date", including all known, undisclosed and unanticipated losses, wrongs, injuries, debts, claims, or damages to PWR, for, upon, or by reason of any matter, cause or thing whatsoever including, but not limited to, any and all matters arising out of my employment by Stanley or the cessation of such employment, and including, but not limited to, any alleged violation of the National Labor Relations Act, Title VII of the Civil Rights Act of 1964, the Civil Rights Act of 1991, Sections 1981 through 1988 of Title 42 of the United States Code, the Employee Retirement Income Security Act of 1974, The Americans with Disabilities Act of 1990, the Age Discrimination in Employment Act of 1967, the Fair Labor Standards Act, the Connecticut Human Rights and Opportunities Law, the Connecticut Minimum Wage Law, the Connecticut Equal Pay Law, and any other federal, state or local civil or human rights law, or any other alleged violation of any

local, state, or federal law, regulation or ordinance, and/or public policy, contract or tort or common-law and any allegations for costs, fees, or other expenses, including attorneys' fees, incurred in these matters; provided that nothing contained herein is intended to prevent me from enforcing the terms and conditions of this Agreement or of the Termination Protection Agreement, pursuing claims for unemployment compensation benefits, or pursuing claims under any retirement, savings or other employee benefit programs to the extent that I have any accrued rights (subject to any modification thereof by the provisions of this Agreement or of the Termination Protection Agreement) thereunder as of my "termination date".

4. I waive my right to file any charge or complaint nor will I accept any relief or recovery from any charge or complaint before any federal, state, or local administrative agency against Stanley, based on any claims, demands, suits, charges, complaints, actions, causes of action, or legal proceedings waived or released pursuant to this Agreement and General Release, except as such waiver is prohibited by law. I further waive all rights to file any action before any federal, state, or local court against Stanley based on any claims, demands, suits, charges, complaints, actions, causes of action, or legal proceedings waived or released pursuant to this Agreement and General Release. I confirm that no such charge, complaint, or action exists in any forum or form. Except as prohibited by law, in the event that any such claim is filed, it shall be dismissed with prejudice upon presentation hereof and I shall reimburse Stanley for the costs, including reasonable attorneys' fees, of defending any such action.

5. I agree not only to release Stanley from any and all claims as stated above which I could make on my own behalf, but also those which may be made by any other person or organization on my behalf. I specifically waive any right to become, and promise not to become, a member of any class in a case in which a claim or claims against Stanley are made involving any events up to and including my "termination date", except where such waiver is prohibited by law. I further waive any right voluntarily to assist in any way any individual or entity in commencing or prosecuting any action or proceeding including, but not limited to, any administrative agency claims, charges, or complaints and/or any lawsuit against Stanley, or in any way to participate or cooperate voluntarily in any such action or proceeding.

6. With respect to any secret or confidential information obtained by me during my employment at Stanley, except with the prior written agreement of Stanley, as required by law, or as may be necessary to defend myself in a legal proceeding (I agree to make every reasonable effort to have any such information covered by a protective order of confidentiality before any such disclosure not covered by the prior written agreement of Stanley), I will not disclose or use for any purpose any such secret or confidential information. For purposes hereof, secret or confidential information shall include, but not be limited to, any process, technique, formula, recipe, drawing, apparatus, method for or result of cost calculation, result of any investigation or experiment made by or on behalf of Stanley, and any sales, production, strategic, or other competitive information, acquired by me during the course of my employment by Stanley and all other information that Stanley itself does not disclose to the public.

I further agree that any work, design, discovery, invention, or improvement conceived, made, developed, or received by me during the period of my employment with Stanley, which relates to the actual or anticipated (as of my "termination date") business, operations, or research of Stanley, including but not limited to any process, art, machine, manufacture, materials, or composition of matter, which could be manufactured or used by Stanley, whether patentable or not, is the sole and exclusive property of Stanley. The terms invention and improvement as used herein, in addition to their customary meaning, shall mean creative concepts and ideas relating to advertising, marketing, promotional, and sales activities.

I further state that I have assigned or hereby do assign to Stanley or its designee all right, title, and interest in any or to any idea, work, design, discovery, invention, or improvement made or created during my employment at Stanley and to any application for letters patent or for trademark registration made thereon, and to any common law or statutory copyright therein. I further agree that I will cooperate with Stanley in order to enable it to secure any patent, trademark, copyright, or other property right therefor in the United States or any foreign country, and any division, renewal, continuation, or continuation-in-part thereof, or for any reissue of any patent issued thereon.

I also agree that Stanley has all rights to, possession of, and all title in and to, all electronic files, papers, documents, and drawings, including copies thereof, which I may have originated or which came into my possession during my employment with Stanley and which related to the business of Stanley, regardless of whether such electronic files, papers, documents, and drawings are kept at my office, at my home, or somewhere else, without retaining any copies thereof.

7. I agree that I shall not make any disparaging remarks or demeaning comment, of any kind or nature, regarding Stanley or any of its officers, directors, agents, or employees.

8. I agree not to disclose any information regarding the substance of this Agreement and General Release. Notwithstanding this agreement of non-disclosure, I may disclose the substance of this Agreement and General Release to my spouse, my children, my accountant, and other financial advisers, and to my attorney or other person with whom I choose to consult concerning the execution of this Agreement and General Release (I agree that I will obtain for the benefit of Stanley the agreement of any such person not to disclose such substance); and I may disclose this Agreement and General Release in connection with any claim I may file for unemployment compensation benefits, to defend myself in a legal proceeding, or as otherwise required by law (I agree to make every reasonable effort to have this Agreement and General Release covered by a protective order of confidentiality before any such disclosure is made in connection with any such defense, or any such requirement of law).

9. I shall not apply in the future for any employment with Stanley.

10. This Agreement and General Release is made in the State of Connecticut and shall

be interpreted under the laws of such state. If any portion of this Agreement and General Release is declared illegal or unenforceable by any court of competent jurisdiction and cannot be modified to be enforceable, including the general release language, such portion shall immediately become null and void, leaving the remainder of this Agreement and General Release in full force and effect. However, if in any proceeding it is asserted by me or anyone else on my behalf and with my approval that any portion of the general release language of paragraphs 3, 4, or 5 is unenforceable and any portion of such language is, in fact, ruled to be unenforceable in such proceeding for any reason, I shall return to Stanley the consideration paid by Stanley under the Termination Protection Agreement.

11. I agree that neither this Agreement and General Release nor the furnishing of the consideration for this Agreement and General Release shall be deemed or construed at any time for any purpose as an admission by Stanley of any liability or unlawful conduct of any kind.

12. This Agreement and General Release may not be modified, altered, or changed except upon express written consent of both Stanley and me wherein specific reference is made to this Agreement and General Release.

13. This Agreement and General Release, together with the Termination Protection Agreement, sets forth the entire agreement between Stanley and me and fully supersedes any prior agreements or understandings between us.

I HAVE READ AND FULLY CONSIDERED THIS AGREEMENT AND GENERAL RELEASE AND I AM DESIROUS OF ENTERING INTO THIS AGREEMENT AND GENERAL RELEASE. THE TERMS OF THIS AGREEMENT AND GENERAL RELEASE ARE THE PRODUCT OF MUTUAL NEGOTIATION AND COMPROMISE BETWEEN STANLEY AND ME AND I UNDERSTAND THAT THIS AGREEMENT AND GENERAL RELEASE SETTLES, BARS, AND WAIVES CLAIMS THAT I HAVE OR COULD POSSIBLY HAVE AGAINST STANLEY. I HAVE BEEN AFFORDED AT LEAST 21 DAYS TO CONSIDER THIS AGREEMENT AND GENERAL RELEASE AND HAVE BEEN ADVISED IN WRITING TO CONSULT WITH AN ATTORNEY PRIOR TO EXECUTION OF THIS AGREEMENT AND GENERAL RELEASE. HAVING ELECTED TO EXECUTE THIS AGREEMENT AND GENERAL RELEASE, TO FULFILL THE PROMISES SET FORTH HEREIN, AND TO RECEIVE THEREBY THE SUMS AND BENEFITS SET FORTH IN PARAGRAPHS 2a THROUGH 2j OF THE TERMINATION PROTECTION

56 Pheasant Chase Road
West Hartford, CT 06117

Date

Mr. Stephen S. Weddle
Vice President and General Counsel
The Stanley Works
1000 Stanley Drive
New Britain, CT 06053

Agreement and General Release

Dear Steve:

On _____, I executed an Agreement and General Release in favor of The Stanley Works. I was advised by The Stanley Works, in writing, to consult with an attorney of my choosing prior to executing such Agreement and General Release.

More than 7 days have elapsed since I executed such Agreement and General Release. I have at no time revoked my acceptance or execution of such Agreement and General Release and I reaffirm my acceptance of such Agreement and General Release. Therefore, in accordance with the terms of such Agreement and General Release, I request payment of the benefits described in paragraphs 2a through 2j of the Termination Protection Agreement referred to therein.

Very truly yours,

Paul W. Russo

Adopted by the Board of Directors September 17, 1997
Amended by the Board of Directors February 25, 1998
[Adopted by the shareholders April 15, 1998]

THE STANLEY WORKS
1997 LONG-TERM INCENTIVE PLAN

Section 1. Purpose

The purposes of this Long-Term Incentive Plan (the "Plan") are to encourage selected salaried employees of The Stanley Works (together with any successor thereto, the "Company") and its Affiliates (as defined below) to acquire a proprietary interest in the growth and performance of the Company, to generate an increased incentive to contribute to the Company's future success and prosperity, thus enhancing the value of the Company for the benefit of its shareholders, and to enhance the ability of the Company and its Affiliates to attract and retain exceptionally qualified individuals upon whom, in large measure, the sustained progress, growth and profitability of the Company depend.

Section 2. Definitions

As used in the Plan, the following terms shall have the meanings set forth below:

- (a) "Affiliate" shall mean (i) any entity that, directly or through one or more intermediaries, is controlled by the Company and (ii) any entity in which the Company has a significant equity interest, as determined by the Committee.
- (b) "Award" shall mean any Option, Stock Appreciation Right, Restricted Stock, Restricted Stock Unit, Performance Award, Dividend Equivalent, or Other Stock-Based Award granted under the Plan.
- (c) "Award Agreement" shall mean any written agreement, contract, or other instrument or document evidencing any Award granted under the Plan.
- (d) "Board of Directors" or "Board" shall mean the Board of Directors of the Company.
- (e) "Code" shall mean the Internal Revenue Code of 1986, as amended from time to time.

- (f) "Committee" shall mean the Compensation and Organization Committee of the Board.
- (g) "Dividend Equivalent" shall mean any right granted under Section 6(e) of the Plan.
- (h) "Exchange Act" shall mean the Securities Exchange Act of 1934, as amended from time to time.
- (i) "Fair Market Value" shall mean, with respect to any property other than Shares, the fair market value of such property determined by such methods or procedures as shall be established from time to time by the Committee, and with respect to Shares, shall mean the mean average of the high and the low price of a Share as quoted on the New York Stock Exchange Composite Tape on the date as of which fair market value is to be determined or, if there is no trading of Shares on such date, such mean average of the high and the low price on the next preceding date on which there was such trading.
- (j) "Immediate family members" of a Participant shall mean the Participant's children, grandchildren and spouse.
- (k) "Incentive Stock Option" shall mean an option granted under Section 6(a) of the Plan that is intended to meet the requirements of Section 422 of the Code, or any successor provision thereto.
- (l) "1990 Plan" shall mean the Company's 1990 Stock Option Plan.
- (m) "Non-Qualified Stock Option" shall mean an option granted under Section 6(a) of the Plan that is not intended to be an Incentive Stock Option.
- (n) "Option" shall mean an Incentive Stock Option or a Non-Qualified Stock Option.
- (o) "Other Stock-Based Award" shall mean any right granted under Section 6(f) of the Plan.
- (p) "Participant" shall mean a Salaried Employee designated to be granted an Award under the Plan.
- (q) "Performance Award" shall mean any Award granted under Section 6(d) of the Plan.
- (r) "Person" shall mean any individual, corporation, partnership, association, joint-stock company, trust, unincorporated organization, or government or political subdivision thereof.

- (s) "Released Securities" shall mean securities that were Restricted Securities with respect to which all applicable restrictions have expired, lapsed, or been waived.
- (t) "Restricted Securities" shall mean securities covered by Awards of Restricted Stock or other Awards under which issued and outstanding Shares are held subject to certain restrictions.
- (u) "Restricted Stock" shall mean any Share granted under Section 6(c) of the Plan.
- (v) "Restricted Stock Unit" shall mean any right granted under Section 6(c) of the Plan that is denominated in Shares.
- (w) "Salaried Employee" shall mean any salaried Employee of the Company or of any Affiliate.
- (x) "Shares" shall mean shares of the common stock of the Company, par value \$2.50 per share, and such other securities or property as may become the subject of Awards, or become subject to Awards, pursuant to an adjustment made under Section 4(b) of the Plan.
- (y) "Stock Appreciation Right" shall mean any right granted under Section 6(b) of the Plan.

Section 3. Administration

Except as otherwise provided herein, the Plan shall be administered by the Committee. Subject to the terms of the Plan and applicable law, the Committee shall have full power and authority to: (i) designate Participants; (ii) determine the type or types of Awards to be granted to each Participant under the Plan; (iii) determine the number of Shares to be covered by (or with respect to which payments, rights, or other matters are to be calculated in connection with) Awards; (iv) determine the terms and conditions of any Award; (v) determine whether, to what extent, and under what circumstances Awards may be settled or exercised in cash, Shares, other securities, other Awards, or other property, or canceled, forfeited, or suspended, and the method or methods by which Awards may be settled, exercised, canceled, forfeited, or suspended; (vi) determine whether, to what extent, and under what circumstances cash, Shares, other securities, other Awards, other property and other amounts payable with respect to an Award under the Plan shall be deferred either automatically or at the election of the holder thereof or of the Committee; (vii) interpret and administer the Plan and any

instrument or agreement relating to, or Award made under, the Plan; (viii) establish, amend, suspend, or waive such rules and regulations and appoint such agents as it shall deem appropriate for the proper administration of the Plan; and (ix) make any other determination and take any other action that the Committee deems necessary or desirable for the administration of the Plan. Unless otherwise expressly provided in the Plan, all designations, determinations, interpretations, and other decisions under or with respect to the Plan or any Award shall be within the sole discretion of the Committee, may be made at any time, and shall be final, conclusive, and binding upon all Persons, including the Company, any Affiliate, any Participant, any holder or beneficiary of any Award, any shareholder, and any employee of the Company or of any Affiliate.

Section 4. Shares Available for Awards

(a) Shares Available. Subject to adjustment as provided in Section 4(b):

- (i) Calculation of Number of Shares Available. The number of Shares authorized to be issued in connection with the granting of Awards under the Plan is four million (4,000,000), and the number of Shares available for granting Awards under the Plan in each fiscal year or, in the case of the years 1997 and 2007, part thereof shall be two percent (2%) of the issued Shares (including, without limitation, treasury Shares) as of the first day of such year; provided, however, that the number of Shares available for granting Awards in any year shall be increased in any such year by the number of Shares available under the Plan in previous years but not covered by Awards granted under the Plan in such years. Further, if any Shares covered by an Award granted under the Plan or by an award granted under the 1990 Plan, or to which such an Award or award relates, are forfeited, or if an Award or award otherwise terminates without the delivery of Shares or of other consideration, or if upon the termination of the 1990 Plan there are Shares remaining that were authorized for issuance under that Plan but with respect to which no awards have been granted, then the Shares covered by such Awards or award, or to which such Award or award relates, or the number of Shares otherwise counted against the aggregate number of Shares available under the Plan with respect to such Award or award,

to the extent of any such forfeiture or termination, or which were authorized for issuance under the 1990 Plan but with respect to which no awards were granted as of the termination of the 1990 Plan shall again be, or shall become available for granting Awards under the Plan. Notwithstanding the foregoing but subject to adjustment as provided in Section 4(b), no more than one million (1,000,000) Shares shall be cumulatively available for delivery pursuant to the exercise of Incentive Stock Options.

(ii) Accounting for Awards. For purposes of this Section 4,

(A) if an Award (other than a Dividend Equivalent) is denominated in Shares, the number of Shares covered by such Award, or to which such Award relates, shall be counted on the date of grant of such Award against the aggregate number of Shares available for granting Awards under the Plan; and

(B) Dividend Equivalents and Awards not denominated in Shares shall be counted against the aggregate number of Shares available for granting Awards under the Plan, if at all, only in such amount and at such time as the Committee shall determine under procedures adopted by the Committee consistent with the purposes of the Plan;

provided, however, that Awards that operate in tandem with (whether granted simultaneously with or at a different time from), or that are substituted for, other Awards or awards granted under the 1990 Plan may be counted or not counted under procedures adopted by the Committee in order to avoid double counting. Any Shares that are delivered by the Company, and any Awards that are granted by, or become obligations of, the Company through the assumption by the Company or an Affiliate of, or in substitution for, outstanding awards previously granted by an acquired company, shall not be counted against the Shares available for granting Awards under the Plan.

(iii) Sources of Shares Deliverable Under Awards. Any Shares delivered pursuant to an Award may consist, in whole or in part, of authorized and unissued Shares or of treasury Shares.

- (b) Adjustments. In the event that the Committee shall determine that any dividend or other distribution (whether in the form of cash, Shares, other securities, or other property), recapitalization, stock split, reverse stock split, reorganization, merger, consolidation split-up, spin-off, combination repurchase, or exchange of Shares or other securities of the Company, issuance of warrants or other rights to purchase Shares or other securities of the Company, or other similar corporate transaction or event affects the Shares such that an adjustment is determined by the Committee to be appropriate in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan, then the Committee shall, in such manner as it may deem equitable, adjust any or all of (i) the number and type of Shares (or other securities or property) which thereafter may be made the subject of Awards, (ii) the number and type of Shares (or other securities or property) subject to outstanding Awards, (iii) the number and type of Shares (or other securities or property) specified as the annual per-participant limitation under Section 6(g)(vi), and (iv) the grant, purchase, or exercise price with respect to any Award, or, if deemed appropriate, make provision for a cash payment to the holder of an outstanding Award; provided, however, in each case, that with respect to Awards of Incentive Stock Options no such adjustment shall be authorized to the extent that such authority would cause the Plan to violate Section 422(b)(1) of the Code or any successor provision thereto; and provided further, however, that the number of Shares subject to any Award denominated in Shares shall always be a whole number.

Section 5. Eligibility

Any Salaried Employee, including any officer or employee- director of the Company or of any Affiliate, who is not a member of the Committee shall be eligible to be designated a Participant.

Section 6. Awards

- (a) Options. The Committee is hereby authorized to grant Options to Participants with the following terms and conditions and with such additional terms and conditions, in either case not inconsistent with the provisions of the Plan, as the Committee shall determine:
- (i) Exercise Price. The purchase price per Share

purchasable under an Option shall be determined by the Committee; provided, however, that such purchase price shall not be less than the Fair Market Value of a Share on the date of grant of such Option (or, if the Committee so determines, in the case of any Option retroactively granted in tandem with or in substitution for another Award or any outstanding award granted under any other plan of the Company, on the date of grant of such other Award or award).

- (ii) Option Term. The term of each Option shall be fixed by the Committee.
- (iii) Time and Method of Exercise. The Committee shall determine the time or times at which an Option may be exercised in whole or in part, and the method or methods by which, and the form or forms, including, without limitation, cash, Shares, other Awards, or other property, or any combination thereof, having a Fair Market Value on the exercise date equal to the relevant exercise price, in which, payment of the exercise price with respect thereto may be made or deemed to have been made.
- (iv) Incentive Stock Options. The terms of any Incentive Stock Option granted under the plan shall comply in all respects with the provisions of Section 422 of the Code, or any successor provision thereto, and any regulations promulgated thereunder.
- (v) Transferability. An Option shall not be transferable other than by will or the laws of descent and distribution or pursuant to a qualified domestic relations order, as defined in the Code, and, during the Participant's lifetime, shall be exercisable only by the Participant, except that the Committee may:
 - (A) permit exercise, during the Participant's lifetime, by the Participant's guardian or legal representative; and
 - (B) permit transfer, upon the Participant's death, to beneficiaries designated by the Participant in a manner authorized

by the Committee, provided that the Committee determines that such exercise and such transfer are consonant with requirements for exemption from Section 16(b) of the Exchange Act and, with respect to an Incentive Stock Option, the requirements of Section 422(b)(5) of the Code; and

- (C) grant Non-Qualified Stock Options that are transferable, or amend outstanding Non-Qualified Stock Options to make them so transferable, without payment of consideration, to immediate family members of the Participant or to trusts or partnerships for such family members.
- (b) Stock Appreciation Rights. The Committee is hereby authorized to grant Stock Appreciation Rights to Participants. Subject to the terms of the Plan and any applicable Award Agreement, a Stock Appreciation Right granted under the Plan shall confer on the holder thereof a right to receive, upon exercise thereof, the excess of (i) the Fair Market Value of one Share on the date of exercise or, if the Committee shall so determine in the case of any such right other than one related to any Incentive Stock Option, at any time during a specified period before or after the date of exercise over (ii) the grant price of the right as specified by the Committee, which shall not be less than the Fair Market Value of one Share on the date of grant of the Stock Appreciation Right (or, if the Committee so determines, in the case of any Stock Appreciation Right retroactively granted in tandem with or in substitution for another Award or any outstanding award granted under any other plan of the Company, on the date of grant of such other Award or award). Subject to the terms of the Plan and any applicable Award Agreement, the grant price, term, methods of exercise, methods of settlement, and any other terms and conditions of any Stock Appreciation Right shall be as determined by the Committee. The Committee may impose such conditions or restrictions on the exercise of any Stock Appreciation Right as it may deem appropriate.
- (c) Restricted Stock and Restricted Stock Units.
 - (i) Issuance. The Committee is hereby authorized to grant Awards of Restricted Stock and Restricted Stock Units to Participants.

- (ii) Restrictions. Shares of Restricted Stock and Restricted Stock Units shall be subject to such restrictions as the Committee may impose (including, without limitation, any limitation on the right to vote a Share of Restricted Stock or the right to receive any dividend or other right or property), which restrictions may lapse separately or in combination at such time or times, in such installments or otherwise, as the Committee may deem appropriate.
 - (iii) Registration. Any Restricted Stock granted under the Plan may be evidenced in such manner as the Committee may deem appropriate, including, without limitation, book-entry registration or issuance of a stock certificate or certificates. In the event any stock certificate is issued in respect of Shares of Restricted Stock granted under the Plan, such certificate shall be registered in the name of the Participant and shall bear an appropriate legend referring to the terms, conditions, and restrictions applicable to such Restricted Stock.
 - (iv) Forfeiture. Except as otherwise determined by the Committee, upon termination of employment (as determined under criteria established by the Committee) for any reason during the applicable restriction period, all Shares of Restricted Stock and all Restricted Stock Units still, in either case, subject to restriction shall be forfeited and reacquired by the Company; provided, however, that the Committee may, when it finds that a waiver would be in the best interests of the Company, waive in whole or in part any or all remaining restrictions with respect to Shares of Restricted Stock or Restricted Stock Units. Unrestricted Shares, evidenced in such manner as the Committee shall deem appropriate, shall be delivered to the holder of Restricted Stock promptly after such Restricted Stock shall become Released Securities.
- (d) Performance Awards. The Committee is hereby authorized to grant Performance Awards to Participants. Subject to the terms of the Plan and any applicable Award Agreement, a Performance Award granted under the Plan (i) may be denominated or payable in cash, Shares

(including without limitation, Restricted Stock), other securities, other Awards, or other property and (ii) shall confer on the holder thereof rights valued as determined by the Committee and payable to, or exercisable by, the holder of the Performance Award, in whole or in part, upon the achievement of such performance goals during such performance periods as the Committee shall establish. Subject to the terms of the Plan and any applicable Awards Agreement, the performance goals to be achieved during any performance period, the length of any performance period, the amount of any Performance Award granted, and the amount of any payment or transfer to be made pursuant to any Performance Award shall be determined by the Committee.

- (e) Dividend Equivalents. The Committee is hereby authorized to grant to Participants Awards under which the holders thereof shall be entitled to receive payments equivalent to dividends or interest with respect to a number of Shares determined by the Committee, and the Committee may provide that such amounts (if any) shall be deemed to have been reinvested in additional Shares or otherwise reinvested. Subject to the terms of the Plan and any applicable Awards Agreement, such Awards may have such terms and conditions as the Committee shall determine.
- (f) Other Stock-Based Awards. The Committee is hereby authorized to grant to Participants such other Awards that are denominated or payable in, valued in whole or in part by reference to, or otherwise based on or related to, Shares (including, without limitation, securities convertible into Shares), as are deemed by the Committee to be consistent with the purposes of the Plan, provided, however, that such grants must comply with applicable law. Subject to the terms of the Plan and any applicable Award Agreement, the Committee shall determine the terms and conditions of such Awards. Shares or other securities delivered pursuant to a purchase right granted under this Section 6(f) shall be purchased for such consideration, which may be paid by such method or methods and in such form or forms, including, without limitation, cash, Shares, other securities, other Awards, or other property, or any combination thereof, as the Committee shall determine, the value of which consideration, as established by the Committee, shall not be less than the Fair Market Value of such Shares or other securities as of the date such purchase right is granted (or, if the Committee so determines, in the case of any such purchase right retroactively granted in tandem with or in substitution for another Award or any outstanding award granted

under any other plan of the Company, on the date of grant of such other Award or award).

(g) General.

- (i) No Cash Consideration for Awards. Awards shall be granted for no cash consideration or for such minimal cash consideration as may be required by applicable law.
- (ii) Awards May Be Granted Separately or Together. Awards may, in the discretion of the Committee, be granted either alone or in addition to, in tandem with, or in substitution for any other Award or any awards granted under any other plan of the Company or any Affiliate. Awards granted in addition to or in tandem with other Awards, or in addition to or in tandem with awards granted under any other plan of the Company or any Affiliate, may be granted either at the same time as or at a different time from the grant of such other Awards or awards.
- (iii) Forms of Payment Under Awards. Subject to the terms of the Plan and of any applicable Award Agreement, payments or transfers to be made by the Company or an Affiliate upon the grant, exercise, or payment of an Award may be made in such form or forms as the Committee shall determine, including, without limitation, cash, Shares, other securities, other Awards, or other property, or any combination thereof, and may be made in a single payment or transfer, in installments, or on a deferred basis, in each case in accordance with rules and procedures established by the Committee. Such rules and procedures may include, without limitation, provisions for the payment or crediting of reasonable interest on installment or deferred payments or the grant or crediting of Dividend Equivalents in respect of installment or deferred payments.
- (iv) Limits on Transfer of Awards. Except as provided in Section 6(a) above regarding Options, no Award (other than Released Securities), and no right under any such Award, shall be assignable, alienable, saleable, or transferable by a Participant otherwise than by will or by the laws of

descent and distribution or pursuant to a qualified domestic relations order, as defined in the Code (or, in the case of an Award of Restricted Securities, to the Company); provided, however, that, if so determined by the Committee, a Participant may, in the manner established by the Committee, designate a beneficiary or beneficiaries to exercise the rights of the Participant, and to receive any property distributable, with respect to any Award upon the demand of the Participant. Each Award, and each right under any Award, shall be exercisable, during the Participant's lifetime, only by the Participant or, if permissible under applicable law, by the Participant's guardian or legal representative. No Award (other than Released Securities), and no right under any such Award, may be pledged, alienated, attached, or otherwise encumbered, and any purported pledge, alienation, attachment, or encumbrance thereof shall be void and unenforceable against the Company or any Affiliate.

- (v) Terms of Awards. The Term of each Award shall be for such period as may be determined by the Committee; provided, however, that in no event shall the term of any Incentive Stock Option exceed a period of ten years from the date of its grant.
- (vi) Per-Person Limitation on Options and SARs. The number of Shares with respect to which Options and SARs may be granted under the Plan to an individual Participant in any three-year period from September 17, 1997 through the end of the term shall not exceed 3,000,000 Shares, subject to adjustment as provided in Section 4(b).
- (vii) Share Certificates. All certificates for Shares or other securities delivered under the Plan pursuant to any Award or the exercise thereof shall be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under the Plan or the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which such

Shares or other securities are then listed, and any applicable Federal or state securities laws, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

- (viii) Maximum Payment Amount. The maximum fair market value of payments to any executive officer made in connection with any long-term performance awards (except for payments made in connection with Options or Stock Appreciation Rights) granted under the 1997 Plan shall not, during any three-year period, exceed two percent of Stanley's shareholders' equity as of the end of the year immediately preceding the commencement of such three-year period.

Section 7. Amendment and Termination

Except to the extent prohibited by applicable law and unless otherwise expressly provided in an Award Agreement or in the Plan:

- (a) Amendments to the Plan. The Board of Directors of the Company may amend, alter, suspend, discontinue, or terminate the Plan, including, without limitation, any amendment, alteration, suspension, discontinuation, or termination that would impair the rights of any Participant, or any other holder or beneficiary of any Award theretofore granted, without the consent of any shareholder, Participant, other holder or beneficiary of an Award, or other Person; provided, however, that, notwithstanding any other provision of the Plan or any Award Agreement, without the approval of the shareholders of the Company no such amendment, alteration, suspension, discontinuation, or termination shall be made that would:
 - (i) increase the total number of Shares available for Awards under the Plan, except as provided in Section 4 hereof; or
 - (ii) permit Options, Stock Appreciation Rights, or other Stock-Based Awards encompassing rights to purchase Shares to be granted with per Share grant, purchase, or exercise prices of less than the Fair Market Value of a Share on the date of grant thereof, except to the extent permitted under Sections 6(a), 6(b), or 6(f) hereof.

- (b) Adjustments of Awards Upon Certain Acquisitions. In the event the Company or any Affiliate shall assume outstanding employee awards or the right or obligation to make future such awards in connection with the acquisition of another business or another corporation or business entity, the Committee may make such adjustments, not inconsistent with the terms of the Plan, in the terms of Awards as it shall deem appropriate in order to achieve reasonable comparability or other equitable relationship between the assumed awards and the Awards granted under the Plan as so adjusted.
- (c) Adjustments of Awards Upon the Occurrence of Certain Unusual or Nonrecurring Events. The Committee shall be authorized to make adjustments in the terms and conditions of, and the criteria included in, Awards in recognition of unusual or nonrecurring events (including, without limitation, the events described in Section 4(b) hereof) affecting the Company, any Affiliate, or the financial statements of the Company or any Affiliate, or of changes in applicable laws, regulations, or accounting principles, whenever the Committee determines that such adjustments are appropriate in order to prevent dilution or enlargement of the benefits or potential benefits to be made available under the Plan.
- (d) Correction of Defects, Omissions and Inconsistencies. The Committee may correct any defect, supply any omission, or reconcile any inconsistency in the Plan or any Award in the manner and to the extent it shall deem desirable to carry the Plan into effect.

Section 8. General Provisions

- (a) No Rights to Awards. No Salaried Employee, Participant or other Person shall have any claim to be granted any Award under the Plan, and there is no obligation for uniformity of treatment of Salaried Employees, Participants, or holders or beneficiaries of Awards under the Plan. The terms and conditions of Awards need not be the same with respect to each recipient.
- (b) Delegation. The Committee may delegate to one or more officers or managers of the Company or any Affiliate, or a committee of such officers or managers, the authority, subject to such terms and limitations as the Committee shall determine, to grant Awards to, or to cancel, modify, waive rights with respect to, alter,

discontinue, suspend or terminate Awards held by, Salaried Employees who are not officers of the Company for purposes of Section 16 of the Exchange Act.

- (c) Withholding. The Company or any Affiliate shall be authorized to withhold from any Award granted or any payment due or transfer made under any Award or under the Plan the amount (in cash, Shares, other securities, other Awards, or other property) of withholding taxes due in respect of an Award, its exercise, or any payment or transfer under such Awards or under the Plan and to take such other action as may be necessary in the opinion of the Company or Affiliate to satisfy all obligations for the payment of such taxes.
- (d) No Limit on Other Compensation Arrangements. Nothing contained in the Plan shall prevent the Company or any Affiliate from adopting or continuing in effect other or additional compensation arrangements, and such arrangements may be either generally applicable or applicable only in specific cases.
- (e) No Right to Employment. The grant of an Award shall not be construed as giving a Participant the right to be retained in the employ of the Company or any Affiliate. Further, the Company or an Affiliate may at any time dismiss a Participant from employment, free from any liability, or any claim under the Plan, unless otherwise expressly provided in the Plan or in any Award Agreement.
- (f) Governing Law. The validity, construction, and effect of the Plan and any rules and regulations relating to the Plan shall be determined in accordance with the laws of the State of Connecticut and applicable Federal law.
- (g) Severability. If any provision of the Plan or any Award is or becomes or is deemed to be invalid, illegal, or unenforceable in any jurisdiction, or as to any Person or Award, or would disqualify the Plan or any Award under any law deemed applicable by the Committee, such provision shall be construed or deemed amended to conform to applicable laws, or if it cannot be so construed or deemed amended without, in the determination of the Committee, materially altering the intent of the Plan or the Award, such provision shall be stricken as to such jurisdiction, Person, or Award, and the remainder of the Plan and any such Award shall remain in full force and effect.
- (h) No Trust or Fund Created. Neither the Plan nor any

Award shall create or be construed to create a trust or separate fund of any kind or a fiduciary relationship between the Company or any Affiliate and a Participant or any other Person. To the extent that any Person acquires a right to receive payments from the Company or any Affiliate pursuant to an Award, such right shall be no greater than the right of any unsecured general creditor of the Company or any Affiliate.

- (i) No Fractional Shares. No fractional Shares shall be issued or delivered pursuant to the Plan or any Award, and the Committee shall determine whether cash, other securities, or other property shall be paid or transferred in lieu of any fractional Shares, or whether such fractional Shares or any rights thereto shall be canceled, terminated, or otherwise eliminated.
- (j) Headings. Headings are given to the Sections and subsections of the Plan solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction or interpretation of the Plan or any provision thereof.

Section 9. Change in Control

- (a) Upon the occurrence of a Change in Control (as hereinafter defined);
 - (i) all Options and Stock Appreciation Rights, whether granted as performance awards or otherwise, shall become immediately exercisable in full for the remainder of their terms, and Grantees shall have the right to have the Company purchase all or any number of such Options or Stock Appreciation Rights for cash for a period of thirty (30) days following a Change in Control at the Option Acceleration Price (as hereinafter defined); and
 - (ii) all restrictions applicable to all Restricted Stock and Restricted Stock Units, whether such Restricted Stock and Restricted Stock Units were granted as performance awards or otherwise, shall immediately lapse and have no effect, and Grantees shall have the right to have the Company purchase all or any number of such Restricted Stock Units and shares of Restricted Stock for cash for a period of thirty (30) days following a Change in Control at the Restricted Stock Acceleration Price (as hereinafter defined).

- (b) (i) The "Restricted Stock Acceleration Price" is the highest of the following on the date of a Change in Control:
- (A) the highest reported sales price of a share of the Common Stock within the sixty (60) days preceding the date of a Change in Control, as reported on any securities exchange upon which the Common Stock is listed,
 - (B) the highest price of a share of the Common Stock reported in a Schedule 13D or an amendment thereto as paid within the sixty (60) days preceding the date of the Change in Control,
 - (C) the highest tender offer price paid for a share of the Common Stock, and
 - (D) any cash merger or similar price paid for a share of the Common Stock.
- (ii) The "Option Acceleration Price" is the excess of the Restricted Stock Acceleration Price over the exercise price of the award, except that for Incentive Stock Options, the Option Acceleration Price is limited to the spread between the Fair Market Value on the date of exercise and the option price.
- (c) A "Change in Control" is the occurrence of any one of the following events:
- (i) any "person," as such term is defined in Section 3(a)(9) and modified and used in Sections 13(d) and 14(d) of the Exchange Act (other than a Grantee, the Company, any trustee or other fiduciary holding securities under an employee benefit plan of the Company (or of any subsidiary of the Company), or any corporation owned, directly or indirectly, by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company), is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 25% or more of the combined voting power of the Company's then outstanding securities;

- (ii) during any period of two consecutive years individuals who at the beginning of such period constitute the Board, and any new director (other than a director designated by a person who has entered into an agreement with the Company to effect a transaction described in clause (i), (iii), (iv) or (v) of this definition) whose election by the Board or nomination for election by the Company's shareholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors at the beginning of the period or whose election or nomination for election was previously so approved, cease for any reason to constitute at least a majority thereof;
- (iii) the shareholders of the Company approve a merger or consolidation of the Company with any other corporation, other than (A) a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than 75% of the combined voting power of the voting securities of the Company or such surviving entity outstanding immediately after such merger or consolidation or (B) a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction) in which no "person" (with the exceptions specified in clause (i) of this definition) acquires 25% or more of the combined voting power of the Company's then outstanding securities;
- (iv) the shareholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets; or
- (v) the Company consummates a merger, consolidation, stock dividend, stock split or combination, extraordinary cash dividend, exchange offer, issuer tender offer or other transaction effecting a recapitalization of the Company (or similar transaction) (the "Transaction") and, in connection with the Transaction, a Designated Downgrading occurs with respect to the unsecured general obligations of the Company (the "Securities"), as described below:

- (A) If the rating of the Securities by both Rating Agencies (defined hereinafter) on the date 60 days prior to the public announcement of the Transaction (a "Base Date") is equal to or higher than BBB Minus (as hereinafter defined), then a "Designated Downgrading" means that the rating of the Securities by either Rating Agency on the effective date of the Transaction (or, if later, the earliest date on which the rating shall reflect the effect of the Transaction) (as applicable, the "Transaction Date") is equal to or lower than BB Plus (as hereinafter defined); if the rating of the Securities by either Rating Agency on a Base Date is lower than BBB Minus, then a "Designated Downgrading" means that the rating of the Securities by either Rating Agency on the Transaction Date has decreased from the rating by such Rating Agency on the Base Date. In determining whether the rating of the Securities has decreased, a decrease of one gradation (+ and - for S&P and 1, 2 and 3 for Moody's, or the equivalent thereof by any substitute rating agency referred to below) shall be taken into account;
- (B) "Rating Agency" means either Standard & Poor's Corporation or its successor ("S&P") or Moody's Investor Service, Inc. or its successor ("Moody's");
- (C) "BBB Minus" means, with respect to ratings by S&P, a rating of BBB- and, with respect to ratings by Moody's, a rating of Baa3, or the equivalent thereof by any substitute agency referred to below;
- (D) "BB Plus" means, with respect to ratings by S&P, a rating of BB+ and, with respect to ratings by Moody's, a rating of BBB3, or the equivalent thereof by any substitute agency referred to below;
- (E) The Company shall take all reasonable action necessary to enable each of the Rating Agencies to provide a rating for the Securities, but, if either or both of the Rating Agencies shall not make such a rating available, a

nationally-recognized investment banking firm shall select a nationally-recognized securities rating agency or two nationally-recognized securities rating agencies to act as substitute rating agency or substitute rating agencies, as the case may be.

Section 10. Effective Date of the Plan

The Plan shall be effective as of September 17, 1997.

Section 11. Term of the Plan

No Award shall be granted under the Plan after September 16, 2007. However, unless otherwise expressly provided in the plan or in an applicable Award Agreement, any Award theretofore granted may extend beyond such date, and the authority of the Committee to amend, alter, or adjust any such Award, or to waive any conditions or rights under any such Award, and the authority of the Board of Directors of the Company to amend the Plan, shall extend beyond such date.

Exhibit 12

THE STANLEY WORKS AND SUBSIDIARIES
COMPUTATION OF EARNINGS TO FIXED CHARGES
(in Millions of Dollars)

| | Fiscal Year Ended | | | | |
|--|-------------------|---------------------|---------------------|---------------------|-------------------|
| | January 3 1998 | December 28 1996 | December 30 1995 | December 31 1994 | January 1 1994 |
| Earnings (loss) before income taxes and cumulative adjustment for accounting change | (\$18.6) | \$174.2 | \$112.8 | \$201.8 | \$148.0 |
| Add: | | | | | |
| Portion of rents representative of interest factor | \$11.6 | \$ 12.2 | \$ 13.4 | \$ 12.7 | \$ 11.7 |
| Interest expense | 24.2 | 27.6 | 35.2 | 33.1 | 31.4 |
| Amortization of expense on long-term debt | 0.2 | 0.2 | 0.3 | 0.2 | 0.4 |
| Amortization of capitalized interest | 0.3 | 0.3 | 0.3 | 0.4 | 0.4 |
| | ----- | ----- | ----- | ----- | ----- |
| Income as adjusted | \$17.7 | \$214.5 | \$162.0 | \$248.2 | \$191.9 |
| | ===== | ===== | ===== | ===== | ===== |
| Fixed charges: | | | | | |
| Interest expense | \$24.2 | \$ 27.6 | \$ 35.2 | \$ 33.1 | \$ 31.4 |
| Amortization of expense on long-term debt | 0.2 | 0.2 | 0.3 | 0.2 | 0.4 |
| Capitalized interest | -- | 0.2 | 0.1 | -- | 0.1 |
| Portion of rents representative of interest factor | 11.6 | 12.2 | 13.4 | 12.7 | 11.7 |
| | ----- | ----- | ----- | ----- | ----- |
| Fixed charges | \$36.0 | \$40.2 | \$49.0 | \$46.0 | \$43.6 |
| | ===== | ===== | ===== | ===== | ===== |
| Ratio of earnings to fixed charges | 0.49 | 5.34 | 3.31 | 5.40 | 4.40 |
| | ===== | ===== | ===== | ===== | ===== |

STANLEY 1997 ANNUAL REPORT

MANAGEMENT REPORT ON RESPONSIBILITY FOR FINANCIAL REPORTING

The management of The Stanley Works is responsible for the preparation, integrity and objectivity of the accompanying financial statements. The statements were prepared in accordance with generally accepted accounting principles. Preparation of financial statements and related data involves our best estimates and the use of judgment. Management also prepared the other information in the Annual Report and is responsible for its accuracy and consistency with the financial statements.

The company maintains a system of internal accounting controls which is designed to provide reasonable assurance, at appropriate cost, as to the reliability of financial records and the protection of assets. This system includes monitoring by a staff of internal auditors. It is further characterized by care in the selection of competent financial managers, by organizational arrangements that provide for delegation of authority and divisions of responsibility and by the dissemination of policies and procedures throughout the company.

Management is also responsible for fostering a strong, ethical climate so that the company's affairs are conducted according to the highest standards of personal and business conduct. This responsibility is reflected in the company's Business Conduct

Guidelines which are publicized throughout the organization. The company has a long-established reputation of integrity in business conduct and maintains a systematic program to assess compliance with these policies.

The adequacy of Stanley's internal accounting controls, the accounting principles employed in its financial reporting and the scope of independent and internal audits are reviewed by the Audit Committee of the Board of Directors, consisting solely of outside directors. Both the independent auditors and our internal auditors have unrestricted access to the Audit Committee, and they meet with it periodically, with and without management present.

January 29, 1998

John M. Trani

John M. Trani
Chairman and
Chief Executive Officer

Theresa F. Yerkes

Theresa F. Yerkes
Vice President, Controller

REPORT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

The Shareholders
The Stanley Works

We have audited the accompanying consolidated balance sheets of The Stanley Works and subsidiaries as of January 3, 1998 and December 28, 1996, and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for each of the three fiscal years in the period ended January 3, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Stanley Works and subsidiaries at January 3, 1998 and December 28, 1996, and the consolidated results of their operations and their cash flows for each of the three fiscal years in the period ended January 3, 1998, in conformity with generally accepted accounting principles.

ERNST & YOUNG LLP

Hartford, Connecticut
January 29, 1998

SUMMARY OF SELECTED FINANCIAL INFORMATION

| Millions of Dollars, (except per share amounts) | 1997(A) | 1996(B) | 1995(C) | 1994 | 1993 | 1992 | 1991 | 1990 |
|---|----------|----------|----------|----------|----------|----------|----------|----------|
| CONTINUING OPERATIONS(D) | | | | | | | | |
| Net sales | \$ 2,670 | \$ 2,671 | \$ 2,624 | \$ 2,511 | \$ 2,273 | \$ 2,196 | \$ 1,942 | \$ 1,956 |
| Earnings (loss) | (42) | 97 | 59 | 125 | 93 | 98 | 97 | 106 |
| Earnings (loss) per share(E) | | | | | | | | |
| Basic | \$ (.47) | \$ 1.09 | \$.66 | \$ 1.40 | \$ 1.03 | \$ 1.07 | \$ 1.12 | \$ 1.26 |
| Diluted | \$ (.47) | \$ 1.08 | \$.66 | \$ 1.38 | \$ 1.01 | \$ 1.06 | \$ 1.11 | \$ 1.25 |
| Percent of Net Sales: | | | | | | | | |
| Cost of sales | 66.8% | 67.2% | 68.2% | 67.1% | 68.3% | 66.8% | 66.0% | 65.3% |
| Selling, general and administrative | 23.5% | 22.8% | 22.5% | 22.3% | 22.5% | 24.0% | 23.8% | 23.7% |
| Interest-net | .6% | .8% | 1.2% | 1.2% | 1.1% | 1.2% | 1.3% | 1.3% |
| Other-net | .8% | .8% | .5% | 1.4% | 1.6% | .8% | .8% | 9% |
| Restructuring and asset write-offs | 8.9% | 1.8% | 3.3% | - | - | - | - | - |
| Earnings (loss) before income taxes | (.7%) | 6.5% | 4.3% | 8.0% | 6.5% | 7.2% | 8.1% | 8.8% |
| Earnings (loss) | (1.6%) | 3.6% | 2.3% | 5.0% | 4.1% | 4.5% | 5.0% | 5.4% |
| OTHER KEY INFORMATION | | | | | | | | |
| Total assets | \$ 1,759 | \$ 1,660 | \$ 1,670 | \$ 1,701 | \$ 1,577 | \$ 1,608 | \$ 1,548 | \$ 1,494 |
| Long-term debt | 284 | 343 | 391 | 387 | 377 | 438 | 397 | 398 |
| Shareholders' equity | \$ 608 | \$ 780 | \$ 735 | \$ 744 | \$ 681 | \$ 696 | \$ 689 | \$ 679 |
| Ratios: | | | | | | | | |
| Current ratio | 1.6 | 2.4 | 2.4 | 2.1 | 2.1 | 2.4 | 2.4 | 2.6 |
| Total debt to total capital | 40.5% | 31.7% | 39.6% | 39.2% | 38.7% | 40.1% | 37.6% | 38.7% |
| Income tax rate | (125.4%) | 44.4% | 47.6% | 37.9% | 37.4% | 37.9% | 38.0% | 38.4% |
| Return on average equity(D),(E) | (6.0)% | 12.8% | 8.0% | 17.6% | 13.5% | 14.1% | 14.1% | 15.8% |
| Common Stock Data: | | | | | | | | |
| Dividends per share | \$.77 | \$.73 | \$.71 | \$.69 | \$.67 | \$.64 | \$.61 | \$.57 |
| Equity per share at year-end | \$ 6.85 | \$ 8.79 | \$ 8.28 | \$ 8.37 | \$ 7.62 | \$ 7.66 | \$ 7.61 | \$ 8.25 |
| Market price--high | 47 3/8 | 32 13/16 | 26 11/16 | 22 7/16 | 23 15/16 | 24 1/16 | 22 | 19 7/8 |
| --low | 28 | 23 5/8 | 17 13/16 | 17 7/16 | 18 15/16 | 16 1/4 | 13 | 13 5/16 |

(TABLE RESTUBBED FROM ABOVE)

| Millions of Dollars, (except per share amounts) | 1989 | 1988 | 1987 |
|---|----------|----------|----------|
| CONTINUING OPERATIONS(D) | | | |
| Net sales | \$ 1,951 | \$ 1,888 | \$ 1,744 |
| Earnings (loss) | 117 | 102 | 96 |
| Earnings (loss) per share(E) | | | |
| Basic | \$ 1.35 | \$ 1.18 | \$ 1.11 |
| Diluted | \$ 1.34 | \$ 1.18 | \$ 1.11 |
| Percent of Net Sales: | | | |
| Cost of sales | 64.8% | 65.6% | 64.7% |
| Selling, general and administrative | 23.0% | 23.0% | 23.4% |
| Interest-net | 1.3% | 1.7% | 1.7% |
| Other-net | 1.0% | .6% | .7% |
| Restructuring and asset write-offs | - | - | - |
| Earnings (loss) before income taxes | 9.9% | 9.1% | 9.5% |
| Earnings (loss) | 6.0% | 5.4% | 5.5% |
| OTHER KEY INFORMATION | | | |
| Total assets | \$ 1,491 | \$ 1,405 | \$ 1,388 |
| Long-term debt | 416 | 339 | 354 |
| Shareholders' equity | \$ 659 | \$ 684 | \$ 626 |
| Ratios: | | | |
| Current ratio | 2.6 | 2.6 | 2.4 |
| Total debt to total capital | 39.6% | 35.0% | 40.9% |
| Income tax rate | 39.6% | 40.8% | 41.7% |
| Return on average equity(D),(E) | 17.3% | 15.5% | |
| Common Stock Data: | | | |
| Dividends per share | \$.51 | \$.46 | \$.41 |
| Equity per share at year-end | \$ 7.66 | \$ 7.99 | \$ 7.30 |
| Market price--high | 19 5/8 | 15 5/8 | 18 5/16 |
| --low | 13 3/4 | 12 3/16 | 10 5/8 |

| Millions of Dollars, (except per share amounts) | 1997(A) | 1996(B) | 1995(C) | 1994 | 1993 | 1992 | 1991 | 1990 |
|---|----------|---------|---------|---------|--------|---------|--------|---------|
| Average shares outstanding (in thousands) | | | | | | | | |
| Basic | 89,470 | 89,152 | 89,043 | 89,550 | 89,871 | 91,405 | 86,532 | 84,384 |
| Diluted | 89,470 | 89,804 | 89,839 | 90,656 | 91,296 | 92,842 | 87,552 | 84,770 |
| Other Information: | | | | | | | | |
| Earnings (loss) from continuing operations | \$ (42) | \$ 97 | \$ 59 | \$ 125 | \$ 93 | \$ 98 | \$ 97 | \$ 106 |
| Loss from discontinued operations | - | - | - | - | - | - | - | - |
| Cumulative effect of accounting change | - | - | - | - | (9) | - | (12) | - |
| Net earnings (loss) | \$ (42) | \$ 97 | \$ 59 | \$ 125 | \$ 84 | \$ 98 | \$ 85 | \$ 106 |
| Net earnings (loss) per share(E) | | | | | | | | |
| Basic | \$ (.47) | \$ 1.09 | \$.66 | \$ 1.40 | \$.94 | \$ 1.07 | \$.98 | \$ 1.26 |
| Diluted | \$ (.47) | \$ 1.08 | \$.66 | \$ 1.38 | \$.92 | \$ 1.06 | \$.97 | \$ 1.25 |
| Average number of employees | 18,377 | 18,903 | 19,784 | 19,445 | 18,988 | 18,650 | 17,420 | 17,784 |
| Shareholders of record at end of year | 18,503 | 17,823 | 16,919 | 17,599 | 20,018 | 20,661 | 21,297 | 22,045 |

| Millions of Dollars, (except per share amounts) | 1989 | 1988 | 1987 |
|---|---------|---------|---------|
| Average shares outstanding (in thousands) | | | |
| Basic | 86,756 | 86,217 | 86,714 |
| Diluted | 87,194 | 86,662 | 87,130 |
| Other Information: | | | |
| Earnings (loss) from continuing operations | \$ 117 | \$ 102 | \$ 96 |
| Loss from discontinued operations | - | - | (10) |
| Cumulative effect of accounting change | - | (13) | - |
| Net earnings (loss) | \$ 117 | \$ 89 | \$ 86 |
| Net earnings (loss) per share(E) | | | |
| Basic | \$ 1.35 | \$ 1.03 | \$ 1.00 |
| Diluted | \$ 1.34 | \$ 1.03 | \$.99 |
| Average number of employees | 18,464 | 18,988 | 19,142 |
| Shareholders of record at end of year | 22,376 | 23,031 | 23,051 |

A Includes charges for restructuring and asset write-offs of \$238.5 million, or \$2.00 per share, related transition costs of \$71.0 million, or \$.51 per share, and a non-cash charge of \$10.6 million, or \$.07 per share, for a stock option grant as specified in the company's employment contract with its chief executive officer.

B Includes charges for restructuring and asset write-offs of \$47.8 million, or \$.43 per share, related transition costs of \$32.9 million, or \$.23 per share, and a non-cash charge of \$7.6 million, or \$.08 per share, for elements of the company's employment contract with its chief executive officer.

C Includes charges for restructuring and asset write-offs of \$85.5 million, or \$.72 per share, and related transition costs of \$9.5 million, or \$.06 per share.

D Excluding the cumulative after-tax effect of accounting changes for postemployment benefits of \$8.5 million, or \$.09 per share, in 1993; postretirement benefits of \$12.5 million, or \$.14 per share, in 1991; and income taxes of \$13.1 million, or \$.15 per share, in 1988.

E Earnings per share and return on average equity excluding restructuring charges, asset write-offs, related transition costs and the charges related to recruitment of a new chief executive officer would have been \$2.11 per share and 19.9% in 1997, \$1.83 per share and 18.9% in 1996 and \$1.45 per share and 16.6% in 1995.

MANAGEMENT'S DISCUSSION AND ANALYSIS

RESULTS OF OPERATIONS

On July 18, 1997 the company announced a major initiative to deliver sustained, profitable growth funded by the reallocation of resources. This initiative and the company's prior restructuring program (called "4X4") have resulted in restructuring charges and restructuring-related transition costs. Restructuring charges include the severance associated with employment reductions, write-downs of assets either disposed of or impaired as a result of the initiatives or other business factors, environmental costs of remediating facilities to be closed or vacated and other similar exit costs. The restructuring-related transition costs are additional costs resulting from these major initiatives that are classified as period operating expenses within cost of sales or selling, general and administrative expense categories. These include the costs of moving production equipment, operating duplicative facilities while transferring production or distribution, consulting costs incurred in planning and implementing changes and other types of costs that have been incurred to facilitate the changes encompassed by the restructuring initiatives. Management judgmentally determines which costs should be classified as transition costs based on the criteria of whether the costs are unusual in nature and are expected to cease when the transition activities related to these initiatives end. Because the presence of restructuring charges and transition costs makes it difficult to see the underlying trends within the company's businesses, the company also presents its results on a pro forma or "core" basis, which excludes these as well as other non-recurring charges incurred in the period. The table provided with this discussion reconciles reported results with pro forma core results and reflects the amount of transition costs and non-recurring charges included in operating results.

SALES

Net sales in 1997 of \$2,670 million were slightly lower than 1996 sales of \$2,671 million. The loss of sales from low-margin businesses that were divested as part of restructuring activities reduced sales by \$107 million or 4%. The negative effects of pricing and foreign currency translation combined to reduce sales by 2%. Volume from ongoing business grew 6% from last year. All of the company's businesses achieved volume growth over the prior year with the overall increase being led by gains in fastening products, doors and carpenters tools. Strong performance was also achieved in the industrial and consumer mechanics tools businesses. Generally strong markets in North America and Europe provided the basis for the sales gains. Net sales increased 2% from 1995 to 1996 despite business and product line divestitures, primarily due to strength in the fastening systems and doors businesses.

GROSS PROFIT

The company reported gross profit of \$886 million in 1997, up \$11 million from 1996. Gross profit, as a percent of sales, increased to 33.2% from 32.8% in 1996 and 31.8% in 1995. These improvements reflect manufacturing efficiencies achieved from higher production volumes and the savings from reduced material costs primarily resulting from the company's centralized procurement activities. These gains were offset by price erosion, particularly in the fastening and hardware businesses; the negative foreign currency translation impact of a stronger dollar; and higher levels of restructuring-related transition costs. Transition costs included in cost of sales increased to \$31 million in 1997 from \$16 million in 1996 and \$4 million in 1995. In 1997 and 1996, these costs primarily related to the implementation of demand flow manufacturing in several facilities and the plant rationalization activities for the tools and fastening systems businesses undertaken as part of the 4X4 initiative.

NET SALES ANALYSIS

| | 1997 Net Sales Changes | | | | | 1996 Net Sales Changes | | | | | 1995 |
|--------------------|------------------------|-------|----------------|------------------|----------|------------------------|-------|----------------|------------------|----------|-----------|
| | 1997 | Price | Unit Volume | Aquis/ Divest | Currency | 1996 | Price | Unit Volume | Aquis/ Divest | Currency | |
| ----- | | | | | | | | | | | |
| Industry Segments | | | | | | | | | | | |
| Tools | | | | | | | | | | | |
| Consumer | \$ 754.0 | - | 6% | (3)% | (3)% | \$ 751.1 | - | 1% | (1)% | (1)% | \$ 756.5 |
| Industrial | 552.2 | 1% | 3% | (1)% | - | 538.7 | 3% | (1)% | (1)% | - | 534.7 |
| Engineered | 717.4 | (1)% | 7% | 1% | (2)% | 686.4 | - | 5% | (4)% | - | 678.3 |
| ----- | | | | | | | | | | | |
| Total Tools | 2,023.6 | - | 5% | (1)% | (2)% | 1,976.2 | 1% | 2% | (2)% | (1)% | 1,969.5 |
| Hardware | 352.2 | (2)% | 6% | - | - | 340.4 | 1% | 4% | - | - | 324.2 |
| Specialty Hardware | 293.7 | (1)% | 7% | (23)% | - | 354.2 | (2)% | 8% | 1% | - | 330.6 |
| ----- | | | | | | | | | | | |
| Consolidated | \$2,669.5 | (1)% | 6% | (4)% | (1)% | \$2,670.8 | - | 3% | (1)% | - | \$2,624.3 |
| ----- | | | | | | | | | | | |
| GEOGRAPHIC AREAS | | | | | | | | | | | |
| United States | \$1,900.6 | (1)% | 5% | (5)% | - | \$1,911.5 | - | 3% | (2)% | - | \$1,884.9 |
| Europe | 423.6 | (1)% | 6% | 1% | (6)% | 421.8 | 1% | 2% | 1% | (2)% | 413.4 |
| Other Areas | 345.3 | 1% | 9% | (5)% | (3)% | 337.5 | 1% | 3% | - | - | 326.0 |
| ----- | | | | | | | | | | | |
| Consolidated | \$2,669.5 | (1)% | 6% | (4)% | (1)% | \$2,670.8 | - | 3% | (1)% | - | \$2,624.3 |
| ----- | | | | | | | | | | | |

In addition, in 1997 the company incurred \$2 million in costs related to task forces that were established for the facility rationalization and outsourcing initiatives announced in July. Excluding transition costs, on a core basis, gross profit margin as a percent of sales increased to 34.4% in 1997 from 33.4% in 1996 and 32.0% in 1995.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses increased to \$628 million in 1997 from \$609 million in 1996 and \$592 million in 1995. These expenses were 23.5% of sales in 1997, 22.8% in 1996 and 22.5% in 1995. The increases in expense were primarily in distribution and administration. Distribution costs were higher reflecting consulting expenses and duplicative facility costs associated with the consolidation of North American order entry and distribution. The increases in administrative expenses include consulting expense for reorganization activities and the excess recruitment and relocation costs associated with significant changes in senior management. In addition, 1997 includes approximately \$11 million related to the 1997 announced initiatives, primarily for consulting, contract labor and other temporary resources used to plan and implement the administrative functional consolidation. Total transition costs were \$40 million in 1997, \$17 million in 1996 and \$5 million in 1995. On a core basis excluding these transition costs, selling, general and administrative expenses would have been 22.0% of sales in 1997 as compared with 22.1% in 1996 and 22.4% in 1995.

INTEREST AND NON-OPERATING EXPENSES

Net interest expense (interest expense less interest income) was \$17 million in 1997, \$23 million in 1996 and \$30 million in 1995. The decrease between 1997 and 1996 reflected lower average debt levels, lower effective borrowing rates and higher interest income. The decrease from 1995 to 1996 was due to lower levels of borrowing and effective interest rates. Net other expense (other non-operating expense less other non-operating income) was \$22 million in both 1997 and 1996 and \$14 million in 1995. Included in 1997 and 1996 are non-cash charges related to the recruitment of the company's chief executive officer. These include an \$11 million charge taken in the second quarter of 1997 to reflect the value of stock options granted and \$8 million in 1996 reflecting the value of stock rights awarded under the terms of a three-year employment contract. Although both awards were granted in December 1996, recognition of the option value was required as of the date of shareholder approval. Excluding those non-recurring charges, Other-net expense on a core basis was \$11 million in 1997 compared with \$15 million in 1996 and \$14 million in 1995.

The company's effective tax rate was significantly affected by non-deductible restructuring charges in 1997, 1996 and 1995 and by the non-deductibility of the 1996 charges for CEO benefits. Excluding these charges the effective rate would have been 37.5% in 1997 and 38% in both 1996 and 1995.

BUSINESS SEGMENT RESULTS

The following discussion on the company's business segment results is presented on a pro forma or core basis. The discussion of core results is intended to provide insight into the underlying business and marketplace conditions that would otherwise be obscured by the increasing levels of transition costs. The accompanying table reconciles reported results with core results and indicates the amount of transition costs and restructuring charges associated with each segment.

Net sales in the Tools segment increased 2%, with a 5% increase in ongoing business volume offset by negative foreign currency translation. All businesses reflected volume gains with particular strength noted in fastener tools and fasteners. While there was no net effect of price changes, increases in the industrial businesses offset the significant erosion experienced by the fastening systems business which resulted from two factors. Highly engineered fastening tools

OPERATING RESULTS: PRO FORMA COMPARATIVE ANALYSIS

| | Reported | Restructuring Charges | 1997 Related Transition Costs* | Pro Forma Core | Pro Forma Core Profit Margin | Reported | Restructuring Charges | 1996 Related Transition Costs* | Pro Forma Core | Pro Forma Core Profit Margin |
|-------------------------------------|-----------|-----------------------|--------------------------------|----------------|------------------------------|----------|-----------------------|--------------------------------|----------------|------------------------------|
| INDUSTRY SEGMENTS | | | | | | | | | | |
| Tools | \$ 61.1 | \$194.8 | \$ 51.9 | \$307.8 | 15.2% | \$ 196.6 | \$ 44.6 | \$ 24.1 | \$ 265.3 | 13.4% |
| Hardware | 16.4 | 17.8 | 12.4 | 46.6 | 13.2% | 42.4 | - | 4.4 | 46.8 | 13.7% |
| Specialty Hardware | (12.3) | 23.5 | 3.3 | 14.5 | 4.9% | 12.2 | 0.3 | 2.3 | 14.8 | 4.2% |
| Total | 65.2 | 236.1 | 67.6 | 368.9 | 13.8% | 251.2 | 44.9 | 30.8 | 326.9 | 12.2% |
| Net corporate expenses | (59.1) | 2.4 | 14.0 | (42.7) | | (48.9) | 2.9 | 9.7 | (36.3) | |
| Interest expense | (24.7) | - | - | (24.7) | | (28.1) | - | - | (28.1) | |
| Earnings (loss) before income taxes | \$ (18.6) | \$238.5 | \$ 81.6 | \$301.5 | | \$ 174.2 | \$ 47.8 | \$ 40.5 | \$ 262.5 | |
| GEOGRAPHIC AREAS | | | | | | | | | | |
| United States | \$ 83.1 | \$145.6 | \$ 53.4 | \$282.1 | 14.8% | \$ 212.5 | \$ 17.2 | \$ 26.2 | \$ 255.9 | 13.4% |
| Europe | (18.5) | 61.8 | 7.6 | 50.9 | 12.0% | 24.8 | 17.1 | 2.5 | 44.4 | 10.5% |
| Other Areas | 0.6 | 28.7 | 6.6 | 35.9 | 10.4% | 13.9 | 10.6 | 2.1 | 26.6 | 7.9% |
| Total | \$ 65.2 | \$236.1 | \$ 67.6 | \$368.9 | 13.8% | \$ 251.2 | \$ 44.9 | \$ 30.8 | \$ 326.9 | 12.2% |

*Included in Net corporate expenses is a charge of \$10.6 million and \$7.6 million for 1997 and 1996, respectively, for items specified in the company's employment contract with its chief executive officer.

have historically been protected from low-cost foreign sourced competition due to a market preference for a higher quality U.S. made product. The recent availability of foreign sourced tools of an acceptable quality resulted in significant pricing pressure for these products. In addition, a strategic price reduction was implemented in Europe in response to marketplace conditions. Despite this competitive pricing environment, core operating profits as a percent of sales increased to 15.2% from 13.4% in 1996 and 11.4% in 1995 due to manufacturing efficiencies from higher production volumes and cost savings realized from restructuring initiatives, primarily the company's centralized procurement activities.

Net sales in the Hardware segment were up 4% overall, despite a 2% decline in price. Pricing in the U.S. was very competitive. Core operating profits were 13.2% of sales, down from 13.7% in 1996. Gains in productivity from volume and restructuring activities, particularly in the Doors business, were more than offset by lower profitability in the Hardware business resulting from the transfer of its distribution to a new consolidated warehouse. Significant start-up difficulties were encountered resulting in both lower volume and higher freight cost. Most of these difficulties were overcome by the end of 1997. Core operating margins of 13.7% in 1996 improved significantly from the 8.5% margin reported in 1995 due to the absence of operational problems in the Home Decor facility in France.

Net sales in the Specialty Hardware segment decreased 23% as a result of the sale of the garage related products business in early 1997. Growth from ongoing businesses in this segment was strong, with a net 6% increase. Core operating margins were 4.9% of sales as compared with 4.2% in 1996 and 6.1% in 1995. The severe competitive pricing environment in the automated door products market, which accounted for the decline in profitability experienced in 1996, has stabilized and 1997 benefited from gains realized from several restructuring initiatives.

GEOGRAPHIC RESULTS

Unit volume gains in sales were realized in all geographic areas. The US and European economies were strong and provided a solid basis for growth. Canada and Latin America both experienced double digit volume gains, however, Asia experienced disappointing declines. Core operating profits were up in all regions.

RESTRUCTURING ACTIVITIES

The company recorded restructuring charges and charges for the write-down of impaired assets associated with its multiple restructuring initiatives of \$239 million in 1997, \$48 million in 1996 and \$86 million in 1995. The 1997 restructuring charge, approximately half of which is severance, is associated with the comprehensive reallocation of resources announced in mid-1997. The amount of the charge is net of \$7 million in gains resulting from businesses divested under the 4X4 restructuring initiative. The objective of the 1997 restructuring initiative is to deliver profitable sales growth on a sustained basis. This growth, fueled by increased spending on new product development, expansion into new ventures and brand development, will be funded by the savings achieved from streamlining operations and reorganizing into a product management structure. The company is transitioning from a portfolio company with 11 fully independent businesses to a single operating entity. Administrative functions such as finance, human resources and information technology are being centralized. Manufacturing and distribution operations are being rationalized. The company plans to reduce facilities: from 83 manufacturing plants to 45 and from 40 distribution centers to 25. The sales organization has been reorganized to eliminate redundant coverage of key customers and channels. Overall, these actions will change the composition of the company's workforce and are expected to reduce net employment levels by approximately 4,500 people.

The total costs anticipated to accomplish these initiatives are \$340 million, of which \$240 million are restructuring charges, recorded in 1997, and \$100 million are transition costs that will be included in operating earnings through mid-1999. The restructuring is expected to yield approximately \$145 million in annual savings all of which will be reinvested in new product development, new ventures, brand development and other areas to stimulate growth. Most of the 1997 initiative projects are targeted to be complete by 1999. Since several projects depend on achieving common systems, which has been delayed due to year 2000 compliance efforts, it is possible that some of these initiatives will not be completed until the end of 2000. However, the delay in timing is not expected to seriously affect the anticipated results of the 1997 restructuring.

Restructuring charges recorded in 1996 and 1995 were associated with the 4X4 initiative. The goal of 4X4 was to reduce the company's cost structure by \$150 million (half of which was to be reinvested) and to reduce working capital and other assets by \$250 million by the end of 1997. The second objective of that program was to achieve net sales of \$4 billion in 1999. The company did achieve the cost and asset reduction targets, however, the objectives for revenue growth were not fully realized. Under that program, seven businesses were divested; four product categories were exited; eleven manufacturing plants, three distribution centers and two support facilities closed; and a salaried workforce reduction occurred.

Reserves recorded for restructuring activities were \$27 million at the beginning of 1997. During 1997 payments of \$28 million were made, primarily for severance. Other than the restructuring charges recorded in 1997, no other significant changes were made to the restructuring accruals, and the ending balance in 1997 was \$167 million of which \$128 million related to severance, \$13 million to environmental costs of remediating facilities to be closed or vacated and \$26 million to other exit costs. Future cash outlays for severance and other payments in any one year are not expected to materially affect the company's liquidity.

FINANCIAL CONDITION

LIQUIDITY, SOURCES AND USES OF CAPITAL

Management has established aggressive growth plans as well as committed the company to funding significant restructuring activities. The company's historically strong cash generating ability, its ample debt capacity and its access to equity markets provide substantial flexibility in meeting both its routine operational needs and its growth and restructuring objectives. Cash flow from operations in 1997 was \$241 million, slightly less than in 1996 but over 25% higher than the prior average ten year period. This operating cash flow was used to reinvest in the business and to pay shareholder dividends.

Capital expenditures were higher than depreciation and amortization for 1997 due partially to the investment in the North American common distribution and order entry system. Capital expenditures in 1998, other than expenditures required for Year 2000 compliance, are expected to equal depreciation and amortization charges of approximately \$80 million.

Stanley has one of the longest records among industrial companies of paying quarterly dividends to shareholders. The company's objective is to increase dividends at the rate of one-half of the company's earnings growth rate, ultimately reaching a dividend payout ratio (dividends divided by earnings per share) of 25%. Dividends of \$.77 per share paid in 1997 represented a 5% increase over 1996 dividends of \$.73 per share.

The company's policy is to offset the dilutive impact of its employee benefit programs (stock awards, options, etc.) through the purchase of shares in the open market. The net activity related to the share repurchase programs was to reduce equity by \$45 million in 1997 and \$29 million in 1996. This activity has increased over the last several years as a result of increases in the amount of options and other awards and the appreciated market price of the stock. It is anticipated that this activity will continue at similar levels.

Business acquisition and divestiture activity during the year resulted in a net \$24 million cash outflow. As described in the restructuring program, several businesses were sold, the largest of which was the garage related products business in 1997. During 1997 the company also acquired the assets of a European fastener business, Atrio Industriale, SpA.

Debt activities consisted of paydowns of scheduled maturities as well as an increase in short term debt to fund working capital needs. In addition, short term debt and cash were higher at the end of the year due to the timing of cash flows from organizational restructuring which will be eliminated in early 1998 as well as some year end interest arbitrage. Overall, the company's borrowing capacity remains very strong. The debt to total capital ratio of 40.5% was inflated due to the recent restructuring charges.

MARKET RISK

Market risk is the potential economic loss that may result from adverse changes in the fair value of financial instruments. The company is exposed to market risk from changes in foreign currency exchange rates and interest rates.

Exposure to foreign currency risk results because the company, through its global businesses, enters into transactions and makes investments denominated in multiple currencies. The company's predominant exposures are in European and Canadian currencies. All cross-currency trade flows arising from sales and procurement activities are consolidated and netted prior to obtaining risk protection, primarily purchased basket options. The company is able to take advantage of its global positioning by using naturally offsetting exposures to reduce the cost of purchasing protection. From time to time, the company also enters into forward exchange contracts to reduce the earnings and cash flow impact of non-functional currency denominated receivables and payables, predominately intercompany transactions. Gains and losses from these hedging instruments offset the gains or losses on the underlying net exposures, assets and liabilities being hedged. The company has also entered into several cross-currency interest rate swaps, primarily to reduce overall borrowing costs, but also providing a partial hedge of the net investments in certain subsidiaries. Sensitivity to foreign currency exposure risk from these financial instruments at the end of fiscal 1997 would have been immaterial based on the potential loss in fair value from a hypothetical 10% adverse movement in all currencies.

The company's exposure to interest rate risk results from its outstanding debt obligations, short term investments and derivative financial instruments employed in the management of its debt portfolio. The debt portfolio is managed to achieve capital structure targets and reduce the overall cost of borrowing by using a combination of fixed and floating rate debt as well as interest rate swaps, caps and cross-currency interest rate swaps. The company's primary exposure to interest risk comes from its floating rate debt in the US, Canada and Europe and is fairly represented by changes in local LIBOR rates. At January 3, 1998, the result of a hypothetical 1% increase in short term LIBOR rates would not have resulted in a material impact on the pretax profit of the company.

The company has access to financial resources and borrowing capabilities around the world. As of year end 1997, the company had approximately \$381 million of unused lines of credit and \$100 million of unissued debt securities registered with the Securities and Exchange Commission. The company believes that its strong financial position, operating cash flows and borrowing capacity provide the financial flexibility necessary to continue its record of annual dividend payments, to invest in the routine needs of its businesses, to make strategic acquisitions and to fund the restructuring and other initiatives encompassed by its growth strategy.

OTHER MATTERS

ENVIRONMENTAL

The company incurs costs related to environmental issues as a result of various laws and regulations governing current operations as well as the remediation of previously contaminated sites. Future laws and regulations are expected to be increasingly stringent and will likely increase the company's expenditures related to routine environmental matters.

The company accrues for anticipated costs associated with investigatory and remediation efforts in accordance with appropriate accounting guidelines which address probability and the ability to reasonably estimate future costs. The liabilities are reassessed whenever circumstances become better defined or remediation efforts and their costs can be better estimated. Subject to the imprecision in estimating future environmental costs, the company believes that any sum it may pay in connection with environmental matters in excess of the amounts recorded will not have a materially adverse effect on its financial position, results of operations or liquidity.

YEAR 2000 SYSTEMS ISSUES

The company has determined that it will need to modify or replace significant portions of its software and some hardware so that its computer systems will function properly with respect to dates in the year 2000 and beyond. The company also has initiated discussion with its significant suppliers, customers and financial institutions to ensure that those parties have appropriate plans to remediate Year 2000 issues where their systems interface with the company's systems or otherwise impact its operations. The company is assessing the extent to which its operations are vulnerable should those organizations fail to properly remediate their computer systems.

The company's comprehensive Year 2000 initiative is being managed internally by a team of experienced professionals. The team's activities are designed to ensure that there is no adverse effect on the company's core business operations and that transactions with customers, suppliers, and financial institutions are fully supported. The initiative encompasses all business systems, including administrative, manufacturing and distribution equipment that utilize microprocessors. Project completion is expected by mid 1999. While the company believes its plans are adequate to address its Year 2000 concerns, many factors could affect its ultimate success including, but not limited to, the continued availability of outside resources. The project is not expected to exceed \$40 to \$50 million in cost, some of which is potentially capitalizable. This cost range is based on management's best estimates, which were derived utilizing assumptions about future events. The results could differ materially from those anticipated subject to uncertainties regarding the availability of resources and the impact of the issue on key suppliers and customers among others.

NEW ACCOUNTING PRONOUNCEMENTS

The FASB issued Statement of Financial Accounting Standards (SFAS) No. 130, "Reporting Comprehensive Income," and SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," in June of 1997. These standards establish new disclosures for comprehensive income and segments and will be effective for fiscal 1998. New disclosures will include a comprehensive income number and reporting operating segments in accordance with internal management structure.

CAUTIONARY STATEMENTS

Certain risks and uncertainties are inherent in the company's ability to achieve operational excellence and deliver sustained, profitable growth to its shareholders as outlined in this Annual Report to Shareholders.

The company's drive for operational excellence is focused on improving customer service, consolidating multiple manufacturing and distribution facilities, outsourcing non-core activities and converting to common systems. The ability to implement the initiatives associated with these goals is dependent on the company's ability to implement the Stanley Production System and to develop and execute comprehensive plans for facility consolidations, the ability of the organization to complete the transition to a product management structure without losing focus on the business, the availability of vendors to perform non-core functions being outsourced, the successful recruitment and training of new employees, the resolution of any labor issues related to closing facilities, the need to respond to significant changes in product demand during the transition and other unforeseen events.

The company's ability to generate sustained, profitable growth is dependent on successfully freeing up resources to fund new product and brand development and new ventures to broaden its markets and to defend market share in the face of intense price competition. Success at developing new products will depend on the ability of the new product development process to foster creativity and identify viable new product ideas as well as the company's ability to attract new product engineers. The achievement of growth through new ventures will depend upon the ability to successfully identify, negotiate, consummate and integrate into operations acquisitions, joint ventures and/or strategic alliances.

The company's ability to achieve and sustain the improvements resulting from these initiatives will be dependent on the extent of pricing pressure and other changes in its competitive markets, the continued consolidation of customers in consumer channels, increasing global competition, changes in trade, monetary and fiscal policies and laws, inflation, currency exchange fluctuations, the impact of currency exchange rates on the competitiveness of products and recessionary or expansive trends in the economies in which the company operates.

BUSINESS SEGMENT INFORMATION

INDUSTRY SEGMENTS

The company operates worldwide in three reportable segments: Tools, Hardware and Specialty Hardware. Additional sales detail is provided for the Consumer, Industrial and Engineered tool categories within the Tools segment.

GEOGRAPHIC AREAS

The company has manufacturing and warehouse facilities and sales offices in the United States, Europe and Other Areas. The company's operations in Europe are principally located in the European Economic Community. Other Areas principally include Canada, Australia, the Far East and Latin America

INDUSTRY SEGMENTS

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|--|-------------------|-------------------|-------------------|
| NET SALES | | | |
| Tools | | | |
| Consumer | \$ 754.0 | \$ 751.1 | \$756.5 |
| Industrial | 552.2 | 538.7 | 534.7 |
| Engineered | 717.4 | 686.4 | 678.3 |
| Total Tools | 2,023.6 | 1,976.2 | 1,969.5 |
| Hardware | 352.2 | 340.4 | 324.2 |
| Specialty Hardware | 293.7 | 354.2 | 330.6 |
| Consolidated | \$ 2,669.5 | \$ 2,670.8 | \$ 2,624.3 |
| OPERATING PROFIT (LOSS) | | | |
| Tools | | | |
| | \$61.1 | \$196.6 | \$154.9 |
| Hardware | 16.4 | 42.4 | 13.4 |
| Specialty Hardware | (12.3) | 12.2 | 17.8 |
| Total | 65.2 | 251.2 | 186.1 |
| Net corporate expenses | (59.1) | (48.9) | (37.6) |
| Interest expense | (24.7) | (28.1) | (35.7) |
| Earnings (loss) before income taxes | \$ (18.6) | \$174.2 | \$ 112.8 |
| IDENTIFIABLE ASSETS | | | |
| Tools | | | |
| | \$ 1,381.2 | \$ 1,268.2 | \$ 1,287.5 |
| Hardware | 185.7 | 178.3 | 174.9 |
| Specialty Hardware | 93.8 | 105.2 | 99.5 |
| | 1,660.7 | 1,551.7 | 1,561.9 |
| General corporate assets | 98.0 | 107.9 | 108.1 |
| Total | \$ 1,758.7 | \$ 1,659.6 | \$ 1,670.0 |
| Capital Expenditures | | | |
| Tools | | | |
| | \$ 67.6 | \$81.0 | \$ 65.4 |
| Hardware | 7.0 | 11.8 | 9.9 |
| Specialty Hardware | 6.0 | 8.3 | 7.2 |
| DEPRECIATION AND AMORTIZATION | | | |
| Tools | | | |
| | 58.0 | 58.7 | 63.6 |
| Hardware | 9.4 | 9.6 | 10.9 |
| Specialty Hardware | 2.6 | 4.1 | 4.1 |

GENERAL INFORMATION

Intercompany sales between geographic areas and between business segments were not significant. Segment information includes allocations of expenses and assets shared by the segments.

In 1997, sales to a major customer were approximately 12% of consolidated sales but were less than 10% in previous years.

Operating profit represents net sales less operating expenses. In computing operating profit, the following have been excluded: net corporate expenses, interest expense and income taxes.

Identifiable assets are those assets used in the company's operations in each segment or area.

GEOGRAPHIC AREAS

(Millions of Dollars)

| | 1997 | 1996 | 1995 |
|--|------|------|------|
|--|------|------|------|

NET SALES

| | | | |
|---------------|------------|------------|------------|
| United States | \$ 1,900.6 | \$ 1,911.5 | \$ 1,884.9 |
| Europe | 423.6 | 421.8 | 413.4 |
| Other Areas | 345.3 | 337.5 | 326.0 |

| | | | |
|--------------|------------|------------|------------|
| Consolidated | \$ 2,669.5 | \$ 2,670.8 | \$ 2,624.3 |
|--------------|------------|------------|------------|

OPERATING PROFIT (LOSS)

| | | | |
|---------------|---------|----------|----------|
| United States | \$ 83.1 | \$ 212.5 | \$ 146.9 |
| Europe | (18.5) | 24.8 | 26.8 |
| Other Areas | .6 | 13.9 | 12.4 |

| | | | |
|-------|---------|----------|----------|
| Total | \$ 65.2 | \$ 251.2 | \$ 186.1 |
|-------|---------|----------|----------|

IDENTIFIABLE ASSETS

| | | | |
|---------------|------------|----------|------------|
| United States | \$ 1,001.6 | \$ 996.0 | \$ 1,028.5 |
| Europe | 389.1 | 321.6 | 314.1 |
| Other Areas | 315.6 | 277.2 | 255.9 |
| Eliminations | (45.6) | (43.1) | (36.6) |

| | | | |
|-------|------------|------------|------------|
| Total | \$ 1,660.7 | \$ 1,551.7 | \$ 1,561.9 |
|-------|------------|------------|------------|

Note: In 1997, 1996 and 1995, restructuring charges of \$194.8 million, \$44.6 million, and \$64.2 million, respectively, were included in the Tools segment; charges of \$17.8 million in 1997 and \$13.6 million in 1995 were included in the Hardware segment; charges of \$23.5 million, \$.3 million, and \$2.0 million, respectively, were included in the Specialty Hardware segment; and charges of \$2.4 million, \$2.9 million, and \$5.7 million, respectively, were included in Net corporate expenses.

In 1997, 1996 and 1995, restructuring charges of \$145.6 million, \$17.2 million and \$55.2 million, respectively, were included in the United States; charges of \$61.8 million, \$17.1 million and \$16.3 million, respectively, were included in Europe; and charges of \$28.7 million, \$10.6 million and \$8.3 million, respectively, were included in Other Areas.

Included in Net corporate expenses for 1997 and 1996 were charges of \$10.6 million and \$7.6 million, respectively, for items specified in the company's employment contract with its chief executive officer.

The "Operating Results: Pro Forma Comparative Analysis" included in the Management's Discussion and Analysis section of this report provides further analysis of the restructuring charges, asset write-offs and related transition costs.

THE STANLEY WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

Fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995
(Millions of Dollars, except per share amounts)

| | 1997 | 1996 | 1995 |
|---|------------|------------|------------|
| NET SALES | \$ 2,669.5 | \$ 2,670.8 | \$ 2,624.3 |
| COSTS AND EXPENSES | | | |
| Cost of sales | 1,783.4 | 1,795.5 | 1,789.7 |
| Selling, general and administrative | 627.7 | 608.5 | 591.7 |
| Interest-net | 16.6 | 22.5 | 30.3 |
| Other-net | 21.9 | 22.3 | 14.3 |
| Restructuring and asset write-offs | 238.5 | 47.8 | 85.5 |
| | 2,688.1 | 2,496.6 | 2,511.5 |
| EARNINGS (LOSS) BEFORE INCOME TAXES | (18.6) | 174.2 | 112.8 |
| INCOME TAXES | 23.3 | 77.3 | 53.7 |
| NET EARNINGS (LOSS) | \$ (41.9) | \$ 96.9 | \$ 59.1 |
| NET EARNINGS (LOSS) PER SHARE OF COMMON STOCK | | | |
| BASIC | \$ (.47) | \$ 1.09 | \$.66 |
| DILUTED | \$ (.47) | \$ 1.08 | \$.66 |

See notes to consolidated financial statements.

THE STANLEY WORKS AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

January 3, 1998 and December 28, 1996
(Millions of Dollars)

| | 1997 | 1996 |
|---|-------------------|-------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 152.2 | \$ 84.0 |
| Accounts and notes receivable | 472.5 | 446.3 |
| Inventories | 301.2 | 338.1 |
| Deferred taxes | 51.1 | 14.0 |
| Other current assets | 28.3 | 28.5 |
| TOTAL CURRENT ASSETS | 1,005.3 | 910.9 |
| PROPERTY, PLANT AND EQUIPMENT | 513.2 | 570.4 |
| GOODWILL AND OTHER INTANGIBLES | 104.1 | 98.9 |
| OTHER ASSETS | 136.1 | 79.4 |
| TOTAL ASSETS | \$ 1,758.7 | \$ 1,659.6 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Short-term borrowings | \$ 80.8 | \$ 4.9 |
| Current maturities of long-term debt | 50.0 | 15.1 |
| Accounts payable | 155.5 | 130.8 |
| Accrued expenses | 336.4 | 230.8 |
| TOTAL CURRENT LIABILITIES | 622.7 | 381.6 |
| LONG-TERM DEBT | 283.7 | 342.6 |
| RESTRUCTURING RESERVES | 67.6 | - |
| OTHER LIABILITIES | 176.9 | 155.3 |
| SHAREHOLDERS' EQUITY | | |
| Preferred stock, without par value: | | |
| Authorized and unissued 10,000,000 shares | | |
| Common stock, par value \$2.50 per share: | | |
| Authorized 200,000,000 shares; | | |
| issued 92,343,410 shares in 1997 and 1996 | 230.9 | 230.9 |
| Retained earnings | 806.6 | 919.0 |
| Foreign currency translation adjustment | (85.3) | (45.5) |
| ESOP debt | (223.8) | (234.8) |
| | 728.4 | 869.6 |
| Less: cost of common stock in treasury (3,555,329 shares in 1997 and 3,623,618 shares in 1996) | 120.6 | 89.5 |
| TOTAL SHAREHOLDERS' EQUITY | 607.8 | 780.1 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | \$ 1,758.7 | \$ 1,659.6 |

See notes to consolidated financial statements.

THE STANLEY WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

Fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995
(Millions of Dollars)

| | 1997 | 1996 | 1995 |
|--|-----------|---------|---------|
| OPERATING ACTIVITIES: | | | |
| Net earnings (loss) | \$ (41.9) | \$ 96.9 | \$ 59.1 |
| Adjustments to reconcile net earnings (loss) to net cash provided by operating activities: | | | |
| Depreciation and amortization | 72.4 | 74.7 | 81.2 |
| Restructuring and asset write-offs | 238.5 | 47.8 | 85.5 |
| Other non-cash items | (17.9) | 38.5 | 32.3 |
| Changes in operating assets and liabilities: | | | |
| Accounts and notes receivable | (38.7) | (28.9) | (23.3) |
| Inventories | 8.6 | (10.5) | (4.5) |
| Accounts payable and accrued expenses | (.7) | 9.5 | (27.8) |
| Income taxes | 21.8 | 24.3 | (24.1) |
| Other | (.9) | 7.6 | (.3) |
| Net cash provided by operating activities | 241.2 | 259.9 | 178.1 |
| INVESTING ACTIVITIES: | | | |
| Capital expenditures | (73.3) | (78.7) | (66.5) |
| Capitalized software | (10.8) | (25.0) | (20.2) |
| Proceeds from sales of businesses | 34.8 | 36.4 | - |
| Business acquisitions | (58.4) | (5.3) | (3.3) |
| Investment in affiliated company | (23.1) | - | - |
| Other | 5.4 | 10.8 | 4.7 |
| Net cash used by investing activities | (125.4) | (61.8) | (85.3) |
| FINANCING ACTIVITIES: | | | |
| Payments on long-term debt | (7.4) | (26.0) | (83.5) |
| Proceeds from long-term borrowings | 2.8 | 2.0 | 86.0 |
| Net short-term financing | 75.3 | (72.3) | (5.1) |
| Proceeds from issuance of common stock | 40.5 | 36.5 | 5.7 |
| Purchase of common stock for treasury | (83.0) | (65.7) | (13.2) |
| Cash dividends on common stock | (68.6) | (67.6) | (75.2) |
| Net cash used by financing activities | (40.4) | (193.1) | (85.3) |
| Effect of exchange rate changes on cash | (7.2) | 3.6 | (1.4) |
| INCREASE IN CASH AND CASH EQUIVALENTS | 68.2 | 8.6 | 6.1 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | 84.0 | 75.4 | 69.3 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | \$ 152.2 | \$ 84.0 | \$ 75.4 |

See notes to consolidated financial statements.

THE STANLEY WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Fiscal years ended January 3, 1998, December 28, 1996 and December 30, 1995

| (Millions of Dollars, except per share amounts) | Common Stock | Capital In Excess of Par Value | Retained Earnings | Foreign Currency Translation Adjustment | ESOP Debt | Treasury Stock | Shareholders' Equity |
|--|-----------------|--------------------------------------|----------------------|--|------------|-------------------|-------------------------|
| BALANCE DECEMBER 31, 1994 | \$ 115.4 | \$ 70.1 | \$ 937.8 | \$ (56.3) | \$ (253.7) | \$ (69.1) | \$ 744.2 |
| Net earnings | | | 59.1 | | | | 59.1 |
| Currency translation adjustment | | | | (14.3) | | | (14.3) |
| Cash dividends declared--\$.71 per share | | | (62.6) | | | | (62.6) |
| Issuance of common stock | | (1.7) | | | | 13.9 | 12.2 |
| Purchase of common stock | | | | | | (16.7) | (16.7) |
| ESOP debt | | | | | 9.4 | | 9.4 |
| ESOP tax benefit | | | 3.3 | | | | 3.3 |
| BALANCE DECEMBER 30, 1995 | 115.4 | 68.4 | 937.6 | (70.6) | (244.3) | (71.9) | 734.6 |
| Two-for-one stock split | 115.5 | (66.9) | (48.6) | | | | - |
| Net earnings | | | 96.9 | | | | 96.9 |
| Currency translation adjustment | | | | 25.1 | | | 25.1 |
| Cash dividends declared--\$.73 per share | | | (65.2) | | | | (65.2) |
| Issuance of common stock | | (6.2) | (5.1) | | | 53.4 | 42.1 |
| Purchase of common stock | | | | | | (71.0) | (71.0) |
| Tax benefit related to stock options | | 4.7 | .3 | | | | 5.0 |
| ESOP debt | | | | | 9.5 | | 9.5 |
| ESOP tax benefit | | | 3.1 | | | | 3.1 |
| Balance December 28, 1996 | 230.9 | - | 919.0 | (45.5) | (234.8) | (89.5) | 780.1 |
| Net loss | | | (41.9) | | | | (41.9) |
| Currency translation adjustment | | | | (39.8) | | | (39.8) |
| Cash dividends declared--\$.77 per share | | | (68.6) | | | | (68.6) |
| Issuance of common stock | | | (13.4) | | | 61.1 | 47.7 |
| Purchase of common stock | | | | | | (92.2) | (92.2) |
| Tax benefit related to stock options | | | 8.7 | | | | 8.7 |
| ESOP debt | | | | | 11.0 | | 11.0 |
| ESOP tax benefit | | | 2.8 | | | | 2.8 |
| BALANCE JANUARY 3, 1998 | \$ 230.9 | \$ - | \$ 806.6 | \$ (85.3) | \$ (223.8) | \$ (120.6) | \$ 607.8 |

See notes to consolidated financial statements.

A. SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The consolidated financial statements include the accounts of the company and its majority-owned subsidiaries which require consolidation, after the elimination of intercompany accounts and transactions. The company's fiscal year ends on the Saturday nearest to December 31. There were 53 weeks in fiscal year 1997 and 52 weeks in fiscal years 1996 and 1995.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, as well as certain financial statement disclosures. While management believes that the estimates and assumptions used in the preparation of the financial statements are appropriate, actual results could differ from these estimates.

FOREIGN CURRENCY TRANSLATION

For most foreign operations, asset and liability accounts are translated at current exchange rates; income and expenses are translated using weighted average exchange rates. Resulting translation adjustments, as well as gains and losses from certain intercompany transactions, are reported in a separate component of shareholders' equity. Translation adjustments for operations in highly inflationary economies and exchange gains and losses on transactions are included in earnings.

CASH EQUIVALENTS

Highly liquid investments with original maturities of three months or less are considered cash equivalents.

INVENTORIES

U.S. inventories are valued at the lower of last-in, first-out (LIFO) cost or market. Other inventories are valued generally at the lower of first-in, first-out (FIFO) cost or market.

LONG-LIVED ASSETS

Property, plant and equipment are stated on the basis of historical cost less accumulated depreciation. Depreciation is provided using a combination of accelerated and straight-line methods over the estimated useful lives of the assets.

Goodwill is amortized on a straight-line basis over periods not exceeding forty years. The company periodically evaluates the existence of goodwill impairment on the basis of whether amounts recorded are recoverable from projected undiscounted cash flows of related businesses. Impairment losses are valued by comparing the carrying value of the goodwill to its fair value, generally determined by the discounted cash flow method.

Impairment losses are recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Impairment losses were charged to operations in 1997, 1996 and 1995 and were included in Restructuring and asset write-offs on the statement of operations.

FINANCIAL INSTRUMENTS

To manage interest rate exposure, the company enters into interest rate swap agreements. The net interest paid or received on the swaps is recognized as interest expense. Gains resulting from the early termination of interest rate swap agreements are deferred and amortized as adjustments to interest expense over the remaining period originally covered by the terminated swap. The company manages exposure to fluctuations in foreign exchange rates by creating offsetting positions through the use of forward exchange contracts or currency options. The company enters into forward exchange contracts to hedge intercompany loans and enters into purchased foreign currency options to hedge anticipated transactions. Gains and losses on forward exchange contracts are deferred and recognized as part of the underlying transactions. Changes in the fair value of options, representing a basket of foreign currencies purchased to hedge anticipated cross-currency cash flows, are included in Other-net expense. The company does not use financial instruments for trading or speculative purposes.

INCOME TAXES

Income tax expense is based on reported earnings (loss) before income taxes. Deferred income taxes reflect the impact of temporary differences between assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes, and are measured by applying enacted tax rates in effect in years in which the differences are expected to reverse.

EARNINGS PER SHARE

In 1997, the company adopted Statement of Financial Accounting Standards

(SFAS) No. 128, "Earnings per Share". This statement specifies the computation, presentation and disclosure requirements for earnings per share. Under SFAS No. 128, basic earnings per share equals net earnings divided by weighted average shares outstanding during the year. Diluted earnings per share includes the impact of common stock equivalents using the treasury stock method when the effect is dilutive. All per share data has been retroactively restated in accordance with SFAS No. 128.

STOCK-BASED COMPENSATION

The company accounts for its employee stock compensation plans under Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, no compensation cost is recognized for stock-based compensation unless the quoted market price of the stock at the grant date is in excess of the amount the employee must pay to acquire the stock. Pro forma disclosures of net earnings and earnings per share, as if the fair value based method of accounting had been applied, are presented in Note J.

RECLASSIFICATIONS

Certain prior years amounts have been reclassified to conform with the current year presentation.

B. ACQUISITIONS

In November 1997, the company acquired the assets of Atrio Industriale, a manufacturer and distributor of pneumatic fastening tools, collated nails, and staples for \$50.8 million. The acquisition was accounted for under the purchase method of accounting, and accordingly, the 1997 consolidated statement of operations includes the operating results from the acquisition date. The fair value of assets acquired and liabilities assumed was \$77.7 million and \$26.9 million, respectively. The acquisition did not have a material pro forma impact on operations.

C. ACCOUNTS AND NOTES RECEIVABLE

Trade receivables are dispersed among a large number of retailers, distributors and industrial accounts in many countries. Adequate provisions have been established to cover anticipated credit losses. At January 3, 1998 and December 28, 1996, allowances for doubtful receivables of \$19.8 million and \$22.5 million, respectively, were applied as a reduction of current accounts and notes receivable. The company believes it has no significant concentrations of credit risk as of January 3, 1998.

The company sells certain domestic accounts receivable under a revolving sales agreement. The proceeds from these sales were \$61.9 million in 1997, \$73.1 million in 1996 and \$71.7 million in 1995.

D. INVENTORIES

| (Millions of Dollars) | 1997 | 1996 |
|-----------------------|----------|----------|
| Finished products | \$ 203.7 | \$ 223.2 |
| Work in process | 51.9 | 61.7 |
| Raw materials | 43.8 | 50.9 |
| Supplies | 1.8 | 2.3 |
| | \$ 301.2 | \$ 338.1 |

Inventories in the amount of \$160.8 million at January 3, 1998 and \$185.2 million at December 28, 1996 were valued at the lower of LIFO cost or market. If LIFO inventories had been valued at FIFO costs, they would have been \$120.3 million higher than reported at both January 3, 1998 and December 28, 1996.

E. PROPERTY, PLANT AND EQUIPMENT

| (Millions of Dollars) | 1997 | 1996 |
|---|---------|---------|
| Land | \$ 34.7 | \$ 39.2 |
| Buildings | 239.7 | 245.1 |
| Machinery and equipment | 833.4 | 872.4 |
| Computer software | 58.3 | 67.7 |
| | 1,166.1 | 1,224.4 |
| Less: accumulated depreciation and amortization | 652.9 | 654.0 |
| | \$513.2 | \$570.4 |

The provisions for depreciation and amortization for 1997, 1996 and 1995 were \$65.2 million, \$65.9 million and \$68.3 million, respectively.

F. GOODWILL AND OTHER INTANGIBLES

Goodwill and other intangibles at the end of each fiscal year, net of accumulated amortization of \$72.2 million and \$69.9 million, were as follows:

| (Millions of Dollars) | 1997 | 1996 |
|-----------------------|---------|---------|
| Goodwill | \$ 79.0 | \$ 78.0 |
| Other | 25.1 | 20.9 |
| | \$104.1 | \$ 98.9 |

G. ACCRUED EXPENSES

| (Millions of Dollars) | 1997 | 1996 |
|---------------------------|---------|---------|
| Payroll and related taxes | \$ 66.3 | \$ 68.2 |
| Insurance | 25.9 | 28.7 |
| Restructuring | 99.7 | 26.9 |
| Income taxes | 34.1 | 21.4 |
| Other | 110.4 | 85.6 |
| | \$336.4 | \$230.8 |

H. LONG-TERM DEBT
AND FINANCING ARRANGEMENTS

| (Millions of Dollars) | | 1997 | 1996 |
|---|----------|----------|----------|
| Notes payable in 2002 | 7.4% | \$ 100.0 | \$ 100.0 |
| Commercial Paper | 5.7% | 89.3 | 89.3 |
| Notes payable in 1998 | 9.0% | 34.8 | 34.8 |
| Notes payable due semiannually to 2005 | 6.2% | 34.3 | 38.2 |
| Industrial Revenue Bonds due in varying amounts to 2010 | 5.8-6.8% | 19.6 | 21.9 |
| ESOP loan guarantees, payable in varying monthly installments through 2001 | 7.7% | 46.5 | 57.5 |
| Other | | 9.2 | 16.0 |
| | | 333.7 | 357.7 |
| Less: current maturities | | 50.0 | 15.1 |
| | | \$ 283.7 | \$ 342.6 |

Commercial paper outstanding at January 3, 1998 of \$89.3 million is classified as non-current pursuant to the company's intention and ability to continue to finance this obligation on a long-term basis.

The company has on file with the Securities and Exchange Commission a shelf registration statement covering the issuance of up to \$200.0 million of debt securities; as of January 3, 1998, \$100.0 million remained unused. The company has unused short and long-term credit arrangements with several banks to borrow up to \$300.0 million at the lower of prime or money market rates. Of this amount, \$150.0 million is long-term. Commitment fees range from .05% to .07%. In addition, the company has short-term lines of credit with numerous foreign banks aggregating \$80.9 million of which \$80.7 million was available at January 3, 1998. Short-term arrangements are reviewed annually for renewal. Of the long-term and short-term lines, \$300.0 million is available to support the company's commercial paper program. The weighted average interest rates on short-term borrowings at January 3, 1998 and December 28, 1996 were 6.4% and 15.6%, respectively.

The company has guaranteed the long-term notes payable to banks of its employee stock ownership plan (ESOP). The guarantee is reflected in the consolidated balance sheets as long-term debt with a corresponding reduction in shareholders' equity.

To manage interest costs and foreign exchange risk, the company maintains a portfolio of interest rate swap agreements. The portfolio includes currency swaps maturing in 1999 that convert \$89.3 million of commercial paper debt into Swiss Franc debt (5.3% weighted average rate). The company also has a currency swap that converts \$34.3 million of variable rate United States dollar debt to variable rate Dutch Guilder debt (4.0% weighted average rate). See Note I for more information regarding the company's interest rate and currency swap agreements.

Aggregate annual maturities of long-term debt for the years 1999 to 2002 are \$17.1 million, \$18.0 million, \$104.7 million and \$119.3 million, respectively. Interest paid during 1997, 1996 and 1995 amounted to \$22.7 million, \$26.0 million and \$33.9 million, respectively.

Commercial paper, utilized to support working capital requirements, classified as current was \$26.9 million and \$1.1 million, as of January 3, 1998 and December 28, 1996, respectively.

I. FINANCIAL INSTRUMENTS

The company's objectives in using debt related financial instruments are to obtain the lowest cost source of funds within an acceptable range of variable to fixed rate debt proportions, and to minimize the foreign exchange risk of obligations. To meet these objectives the company enters into interest rate swap and currency swap agreements. A summary of instruments and weighted average interest rates follows. The weighted average variable pay and receive rates are based on rates in effect at the balance sheet dates. Variable rates are generally based on LIBOR or commercial paper rates with no leverage features.

| (Millions of Dollars) | 1997 | 1996 |
|-------------------------------------|-----------|-----------|
| ----- | | |
| Interest rate swaps | | |
| Receive fixed-pay variable rates \$ | 50.0 | \$ 50.0 |
| pay rate | 5.7% | 5.5% |
| receive rate | 6.2% | 6.2% |
| maturity dates | 2002 | 2002 |
| Receive variable-pay fixed rates \$ | 88.0 | \$ 23.1 |
| pay rate | 4.4% | 4.4% |
| receive rate | 5.8% | 5.5% |
| maturity dates | 1999 | 1999 |
| Currency swaps | \$ 105.5 | \$149.7 |
| pay rate | 4.2% | 4.5% |
| receive rate | 5.9% | 5.8% |
| maturity dates | 1999-2005 | 1999-2005 |
| ----- | | |

The company uses purchased currency options to reduce exchange risks arising from cross-border cash flows expected to occur over the next one year period. In addition, the company enters into forward exchange contracts to hedge intercompany loans. The objective of these practices is to minimize the impact of foreign currency fluctuations on operating results. At January 3, 1998 and December 28, 1996, the company had forward contracts hedging intercompany loans totaling \$15.6 million and \$14.5 million, respectively. At January 3, 1998 and December 28, 1996, currency basket options hedged anticipated transactions totaling \$166.0 million and \$131.4 million, respectively. The forward contracts and options are primarily denominated in Canadian dollars, Australian dollars, Taiwanese dollars, and major European currencies and generally mature within the next one year period.

The counterparties to these interest rate and currency financial instruments are major international financial institutions. The company is exposed to credit risk for net exchanges under these agreements, but not for the notional amounts. The company considers the risk of default to be remote.

A summary of the carrying values and fair values of the company's financial instruments at January 3, 1998 and December 28, 1996 is as follows:

| (Millions of Dollars) | 1997 | | 1996 | |
|---|----------------|------------|----------------|------------|
| | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Long-term debt, including current portion | \$334.3 | \$336.6 | \$350.4 | \$355.4 |
| Currency and interest rate swaps (.6) | | (.8) | 7.3 | 8.3 |
| | \$333.7 | \$335.8 | \$357.7 | \$363.7 |

Generally, the carrying value of the debt related financial instruments is included in the balance sheet in long-term debt. The fair values of long-term debt are estimated using discounted cash flow analysis, based on the company's marginal borrowing rates. The fair values of foreign currency and interest rate swap agreements are based on current settlement values. The carrying amount of cash equivalents and short-term borrowings approximates fair value.

J. CAPITAL STOCK

STOCK SPLIT

On April 17, 1996, the shareholders approved an increase in the number of authorized common shares from 110,000,000 to 200,000,000. On that date, the Board of Directors declared a two-for-one common stock split to be effected by the distribution of one additional share for each share outstanding. Such distribution was made on June 3, 1996 to shareholders of record as of May 13, 1996. Accordingly, the stock split was recognized by reclassifying \$115.5 million, the par value of the additional shares resulting from the split, from capital in excess of par value and retained earnings to common stock. All shares outstanding and per share amounts were restated to reflect the stock split.

EARNINGS PER SHARE COMPUTATION

The company adopted SFAS No. 128 in 1997 (see note A). The following table reconciles the weighted average shares outstanding used to calculate basic and diluted earnings per share.

| (Millions of dollars, except share and per share amounts) | 1997 | 1996 | 1995 |
|---|------------|------------|------------|
| Net earnings (loss)- basic and diluted | \$ (41.9) | \$ 96.9 | \$ 59.1 |
| Basic earnings per share- weighted average shares | 89,469,849 | 89,151,668 | 89,043,185 |
| Dilutive effect of employee stock options | - | 652,349 | 795,454 |
| Diluted earnings per share- weighted average shares | 89,469,849 | 89,804,017 | 89,838,639 |
| Earnings (loss) per share: | | | |
| Basic | \$ (.47) | \$ 1.09 | \$.66 |
| Diluted | \$ (.47) | \$ 1.08 | \$.66 |

The effect of employee stock options for 1997 was 1,002,456 shares. These shares are not included in the calculations since they are antidilutive.

COMMON STOCK SHARE ACTIVITY

The activity in common shares for each year, net of treasury stock, was as follows:

| | 1997 | 1996 | 1995 |
|---------------------------------|-------------|-------------|------------|
| Outstanding, beginning of year | 88,719,792 | 88,758,830 | 88,898,750 |
| Issued for employee stock plans | 2,239,606 | 2,465,416 | 698,592 |
| Purchased | (2,171,317) | (2,504,454) | (838,512) |
| Outstanding, end of year | 88,788,081 | 88,719,792 | 88,758,830 |

COMMON STOCK RESERVED

At January 3, 1998 and December 28, 1996, the number of shares of common stock reserved for future issuance under various employee and director stock plans was as follows:

| | 1997 | 1996 |
|--------------------------------|------------|------------|
| Employee Stock Purchase Plan | 4,666,251 | 5,400,288 |
| Stock Option Plans | 7,673,877 | 9,039,112 |
| Long-Term Stock Incentive Plan | 2,833,335 | 2,895,066 |
| | 15,173,463 | 17,334,466 |

PREFERRED STOCK PURCHASE RIGHTS

Each outstanding share of common stock has one half of a share purchase right. Each purchase right may be exercised to purchase one two-hundredth of a share of Series A Junior Participating Preferred Stock at an exercise price of \$220.00, subject to adjustment. The rights, which do not have voting rights, expire on March 10, 2006, and may be redeemed by the company at a price of \$.01 per right at any time prior to the 10th day following the public announcement that a person has acquired beneficial ownership of 10% or more of the outstanding shares of common stock.

In the event that the company is acquired in a merger or other business combination transaction, provision shall be made so that each holder of a right (other than a holder who is a 10%-or-more shareholder) shall have the right to receive, upon exercise thereof, that number of shares of common stock of the surviving company having a market value equal to two times the exercise price of the right. Similarly, if anyone becomes the beneficial owner of more than 10% of the then outstanding shares of common stock (except pursuant to an offer for all outstanding shares of common stock which the independent directors have deemed to be fair and in the best interest of the company), provision will be made so that each holder of a right (other than a holder who is a 10%-or-more shareholder) shall thereafter have the right to receive, upon exercise thereof, common stock (or, in certain circumstances, cash, property or other securities of the company) having a market value equal to two times the exercise price of the right. At January 3, 1998, there were 44,394,041 outstanding rights. There are 250,000 shares of Series A Junior Participating Preferred Stock reserved for issuance in connection with the rights.

STOCK OPTIONS AND AWARDS

The company has a stock option plan for officers and key employees that provides for nonqualified and incentive stock option grants. The company also has a stock option plan that provides for option grants to outside directors of the company. Options are granted at the market price of the company's stock on the date of grant and have a maximum term of 10 years.

In December 1996, the company recruited a new Chairman and Chief Executive Officer pursuant to a three year employment agreement. In addition to a base salary, bonus and other annual benefits, 200,000 common stock equivalent share units, and an option grant to purchase 1,000,000 shares at \$27.562 (the market value on the date of issuance) were awarded under the employment agreement. Each share unit had a market value of \$27.75 on the date of the grant and represents the right to receive one share of common stock. The share units will be distributed in three equal annual installments beginning in 2000. In fiscal year 1996, the fair market value of the share units at their grant date was charged to operations and included in Other-net expense in the Statement of Operations. The option, which was approved by shareholders on April 23, 1997 at the Annual Meeting, has a ten year term and is exercisable after June 1997. Fiscal year 1997 includes a charge to operations representing the difference between the exercise price and the fair market value as of the shareholder approval date (effective grant date).

Information regarding the company's stock option plans is summarized below:

| | 1997 | | 1996 | | 1995 | |
|----------------------------------|-------------|---------------------------------|-------------|---------------------------------|-----------|---------------------------------|
| | Options | Weighted Average Exercise Price | Options | Weighted Average Exercise Price | Options | Weighted Average Exercise Price |
| Outstanding, beginning of year | 3,784,738 | \$21.68 | 4,821,194 | \$18.34 | 4,261,602 | \$16.84 |
| Granted | 1,966,000 | 35.34 | 973,450 | 27.95 | 1,098,600 | 23.00 |
| Exercised | (1,365,235) | 20.13 | (1,973,230) | 16.61 | (469,814) | 15.88 |
| Forfeited | (141,490) | 22.21 | (36,676) | 21.29 | (69,194) | 16.33 |
| Outstanding, end of year | 4,244,013 | \$28.49 | 3,784,738 | \$21.68 | 4,821,194 | \$18.34 |
| Options exercisable, end of year | 3,285,513 | \$24.13 | 2,811,288 | \$19.51 | 3,722,594 | \$16.96 |

Options outstanding as of January 3, 1998 had exercised prices as follows: 899,153 options ranging from \$15.06 to \$20.19, 2,378,860 options ranging from \$23.00 to \$28.88 and 966,000 options ranging from \$38.25 to \$44.41. The weighted average remaining contractual life of these options is 8.6 years.

EMPLOYEE STOCK PURCHASE PLAN

The Employee Stock Purchase Plan enables substantially all employees in the United States and Canada to subscribe at any time to purchase shares of common stock on a monthly basis at the lower of 85% of the fair market value of the shares on the first day of the plan year (\$37.19 per share for fiscal year 1998 purchases) or 85% of the fair market value of the shares on the last business day of each month. A maximum of 6,000,000 shares are authorized for subscription. During 1997, 1996 and 1995 shares totaling 734,037, 442,960 and 156,752, respectively, were issued under the plan at average prices of \$23.69, \$19.61 and \$17.29 per share, respectively.

LONG-TERM STOCK INCENTIVE PLAN

The Long-Term Stock Incentive Plan provides for the granting of awards to senior management employees for achieving company performance measures over five year cycles. The Plan is administered by the Compensation and Organization Committee of the Board of Directors consisting of non-employee directors. Awards are payable in shares of common stock as directed by the Committee. The amounts of \$3.5 million, \$2.5 million and \$4 million were charged to expense in 1997, 1996 and 1995, respectively. Shares totaling 61,731, 14,252 and 47,734 were issued in 1997, 1996 and 1995, respectively. The Compensation and Organization Committee determined in 1994 not to make any further awards under this plan. Accordingly, there will be no further payments under this plan subsequent to the 1993-1997 and 1994-1998 award cycles.

STOCK COMPENSATION PLANS

The company accounts for stock option grants under its two stock-based compensation plans and stock purchases under the Employee Stock Purchase Plan in accordance with APB No. 25. Accordingly, no compensation cost has been recognized for the majority of stock option grants since the options have exercise prices equal to the market value of the company's common stock at the date of grant. If compensation cost for the company's stock-based compensation plans had been determined based on the fair value at the grant dates consistent with the method prescribed by SFAS No. 123, "Accounting for Stock-Based

Compensation", the company's net earnings (loss) and earnings (loss) per share would have been adjusted to the pro forma amounts indicated below:

| | 1997 | 1996 | 1995 |
|--|-----------|---------|---------|
| Pro forma net earnings (loss) (in millions) | \$ (56.1) | \$ 90.4 | \$ 55.9 |
| Pro forma earnings (loss) per share: | | | |
| Basic | \$ (.63) | \$ 1.01 | \$.63 |
| Diluted | \$ (.63) | \$ 1.01 | \$.62 |

During the initial phase-in period, as required by SFAS No. 123, the pro forma amounts were determined based on the stock option grants and employee stock purchases subsequent to January 1, 1995. Therefore, the pro forma amounts may not be indicative of the effects of compensation cost on net earnings (loss) and earnings (loss) per share in future years. Pro forma compensation cost relating to the stock options is recognized over the six month vesting period, while Employee Stock Purchase Plan compensation cost is recognized on the first day of the plan year. The fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 1997, 1996 and 1995, respectively: dividend yield of 1.8%, 2.6% and 3.1%; expected volatility of 25% for all years; risk-free interest rates of 6.0%, 6.1% and 6.2%; and expected lives of 7 years. The weighted average fair value of stock options granted in 1997, 1996 and 1995 was \$15.39, \$8.02 and \$6.18, respectively. The fair value of the employees' purchase rights under the Employee Stock Purchase Plan was estimated using the following assumptions for 1997, 1996 and 1995, respectively: dividend yield of 1.8%, 2.6% and 3.1%; expected volatility of 25% for all years; risk-free interest rates of 6.0%, 5.6% and 5.8%; and expected lives of 1.2 years. The weighted average fair value of those purchase rights granted in 1997, 1996 and 1995 was \$8.53, \$6.44 and \$5.65, respectively.

K. EMPLOYEE BENEFIT PLANS

EMPLOYEE STOCK OWNERSHIP PLAN (ESOP)

The Savings Plan provides opportunities for tax-deferred savings, enabling eligible U.S. employees to acquire a proprietary interest in the company. Such employees may contribute from 1% to 15% of their salary to the Plan. The company contributes an amount equal to one-half of the first 7% of employee contributions. The amounts in 1997, 1996 and 1995 under this matching arrangement were \$8.2 million, \$8.4 million and \$8.3 million, respectively.

Shares of the company's common stock held by the ESOP were purchased with the proceeds of external borrowings in 1989 and borrowings from the company in 1991. The external ESOP borrowings are guaranteed by the company and are included in long-term debt. Shareholders' equity reflects both the internal and the external borrowing arrangements.

Shares are released to participant accounts based on principal and interest payments of the underlying debt. These shares along with allocated dividends and shares purchased on the open market are assigned to fund share requirements of the employee contributions, the associated employer match and the dividends earned on participant account balances.

Net ESOP activity recognized is based on total debt service and share purchase requirements less employee contributions and dividends on ESOP shares. The company's net ESOP activity resulted in income of \$15.2 million in 1997, \$8.6 million in 1996 and \$2.6 million in 1995.

Dividends on ESOP shares, which are charged to shareholders' equity as declared, were \$15.2 million, \$15.1 million and \$14.8 million in 1997, 1996 and 1995, respectively. Interest costs incurred by the ESOP on external debt for 1997, 1996 and 1995 were \$4.0 million, \$4.8 million and \$5.5 million, respectively. ESOP shares not yet allocated to participants are treated as outstanding for purposes of computing earnings per share. As of January 3, 1998, the number of ESOP shares allocated to participant accounts was 8,954,931 and the number of unallocated shares was 10,007,568.

PENSION PLANS

The company sponsors non-contributory defined benefit pension plans covering substantially all employees. Benefits for salaried and non-union hourly employees are generally based on salary and years of service, while those for collective bargaining employees are based on a stated amount for each year of service. Additionally, the company contributes to several union-sponsored multi-employer plans which provide defined benefits.

The company's funding policy is to contribute amounts determined annually on an actuarial basis to provide for current and future benefits in accordance with federal law and other regulations. Plan assets are invested in equity securities, bonds, real estate and money market instruments. If the plans are terminated or merged with another plan within three years following a change in control of the company, any excess plan assets are to be applied to increase the benefits of all participants.

Total pension expense includes the following components:

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|-------------------------------|---------|---------|---------|
| Defined benefit plans: | | | |
| Service cost | \$ 22.5 | \$ 20.8 | \$ 16.7 |
| Interest cost | 31.2 | 31.1 | 29.8 |
| Actual return on plan assets | (84.0) | (51.2) | (39.5) |
| Net amortization and deferral | 48.5 | 17.8 | 6.5 |
| Curtailement loss | 5.7 | - | - |
| Net pension expense | 23.9 | 18.5 | 13.5 |
| Multi-employer plans | .8 | .8 | .8 |
| Total pension expense | \$ 24.7 | \$ 19.3 | \$ 14.3 |

In 1997 the company recognized a \$5.7 million pension curtailment loss as part of restructuring charges. This curtailment arose from plant rationalization initiatives as well as the sale of the company's garage related products business.

The funded status of the company's defined benefit plans at the end of each fiscal year was as follows:

| (Millions of Dollars) | 1997 | | 1996 | |
|---|--|--|--|--|
| | Plans Where Assets Exceed Accumulated Benefits | Plans Where Accumulated Benefits Exceed Assets | Plans Where Assets Exceed Accumulated Benefits | Plans Where Accumulated Benefits Exceed Assets |
| Actuarial present value of benefit obligations: | | | | |
| Vested | \$ 326.5 | \$ 12.9 | \$ 351.4 | \$ 13.3 |
| Non-vested | 40.1 | 6.7 | 6.0 | 2.7 |
| Accumulated benefit obligation | 366.6 | 19.6 | 357.4 | 16.0 |
| Additional amounts related to projected pay increases | 72.5 | 6.1 | 69.6 | 6.8 |
| Total projected benefit obligation (PBO) | 439.1 | 25.7 | 427.0 | 22.8 |
| Plan assets at fair value | 518.5 | 7.1 | 463.1 | 7.1 |
| Assets in excess of (less than) PBO | 79.4 | (18.6) | 36.1 | (15.7) |
| Unrecognized net (gain) or loss at transition | (4.7) | .1 | (6.5) | .1 |
| Unrecognized net (gain) or loss | (61.9) | 2.6 | (16.4) | 4.2 |
| Unrecognized prior service cost | 8.2 | 5.8 | 11.3 | 2.7 |
| Adjustment required to recognize minimum liability | - | (4.2) | - | (2.5) |
| Prepaid (accrued) pension expense | \$ 21.0 | \$ (14.3) | \$ 24.5 | \$(11.2) |

Assumptions used for significant defined benefit plans were as follows:

| | 1997 | 1996 | 1995 |
|------------------------------------|------|------|------|
| Discount rate | 7.0% | 7.0% | 7.0% |
| Average wage increase | 4.5% | 4.5% | 4.5% |
| Long-term rate of return on assets | 9.0% | 9.0% | 9.0% |

POSTRETIREMENT BENEFITS

The company provides medical and dental benefits for certain retired employees in the United States. In addition, domestic employees who retire from active service are eligible for life insurance benefits.

The status of the company's plans at the end of each fiscal year was as follows:

| (Millions of Dollars) | 1997 | 1996 |
|--|--------|--------|
| Accumulated postretirement benefit obligation: | | |
| Retirees | \$11.5 | \$13.3 |
| Fully eligible active plan participants | 1.9 | 1.8 |
| Other active plan participants | 4.1 | 3.1 |
| Unrecognized net loss | 17.5 | 18.2 |
| | (1.9) | (2.0) |
| Accrued postretirement benefit expense | \$15.6 | \$16.2 |

Net periodic postretirement benefit expense was \$1.9 million in 1997, \$2.0 million in 1996 and \$2.9 million in 1995.

The weighted average annual assumed rate of increase in the per-capita cost of covered benefits (i.e. health care cost trend rate) is assumed to be 9% for 1998 reducing gradually to 6% by 2010 and remaining at that level

thereafter. A one percentage point increase in the assumed health care cost trend rate would have increased the accumulated benefit obligation by \$.9 million at January 3, 1998 and net periodic postretirement benefit expense for fiscal year 1997 by \$.1 million. A weighted average discount rate of 7% was used in measuring the accumulated benefit obligations in both 1997 and 1996.

L. OTHER COSTS AND EXPENSES

Interest-net for 1997, 1996 and 1995 included interest income of \$8.1 million, \$5.5 million and \$5.3 million, respectively.

Other-net in 1997 includes a non-cash charge of \$10.6 million (\$.07 per share), representing the difference between the exercise price and the fair market value of a 1,000,000 share option grant under terms of the company's employment contract with its chief executive officer. This contract resulted in a 1996 charge of \$7.6 million (\$.08 per share) for the issuance of 200,000 common stock equivalent share units and other immediately vested benefits.

Advertising costs are expensed as incurred and amounted to \$48.2 million in 1997, \$52.5 million in 1996 and \$54.3 million in 1995.

M. RESTRUCTURING AND ASSET WRITE-OFFS

In 1997, the company announced a restructuring initiative to streamline its manufacturing, sales, distribution and administration operations, reducing its overall cost structure. The company will reduce manufacturing and distribution facilities locations from 123 to 70. Many of the closures will be effected by consolidating operations into other company facilities, others by outsourcing work to vendors. In addition, the company reorganized its operations into a product management structure, in which eight product groups will be focusing on customers and sales growth through development of new products and expanding market shares. In support of this structure, manufacturing, engineering, sales and service, finance, human resource and information technology functions will be centralized. The implementation of these restructuring initiatives will also result in additional transition costs, which are expected to be incurred through mid-1999. In 1997, restructuring and asset write-off charges of \$238.5 million included the write-down of assets (\$73.6 million), severance for the termination of approximately 8,900 employees (\$139.3 million), other exit costs (\$32.2 million) and gains on the divestiture of two businesses (\$6.6 million). Pursuant to this restructuring plan, the company terminated 892 employees in 1997. Severance and other exit payments of \$14.2 million were made during the year. At January 3, 1998, reserve balances related to the 1997 restructuring activities were \$201.0 million, of which \$40.9 million relate to the write-down of impaired assets.

In 1996, the company recorded restructuring and asset write-off charges of \$47.8 million for the write-down of assets, severance for approximately 695 employees and other costs associated with a previous restructuring initiative announced in fiscal 1995. Such costs and asset write-offs were primarily related to transfers of production among existing manufacturing facilities, plant closures and resulting workforce reductions (\$35.4 million), and impairment of assets related to restructuring initiatives and strategy changes (\$9.4 million). The company also divested five businesses during 1996 and recognized an associated net loss of \$3.0 million which was included in 1996 restructuring charges.

In 1995, restructuring and asset write-off charges of \$85.5 million included the write-off of assets, severance for approximately 900 employees and other costs. Such costs and asset write-offs were primarily related to exiting three product categories, closing six manufacturing plants, three distribution centers and two support facilities (\$53.4 million), and impairment of assets related to restructuring initiatives and strategy changes (\$20.7 million). Restructuring charges also included \$5.3 million for severance related to a workforce reduction and \$6.1 million for a comprehensive SKU reduction program.

The 1996 and 1995 restructuring initiatives are nearing completion. During 1997 and 1996, payments of \$13.7 million and \$17.9 million, respectively, were made for severance and other exit costs. At January 3, 1998, the reserve balance for these initiatives was \$7.2 million, and is expected to be utilized by the end of 1998.

N. OPERATIONS BY INDUSTRY SEGMENT
AND GEOGRAPHIC AREA

Industry Segment and Geographic Area information included on page 19 of this report is an integral part of the financial statements.

O. INCOME TAXES

Significant components of the company's deferred tax liabilities and assets as of the end of each fiscal year were as follows:

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|---------------------------------------|---------|---------|----------|
| ----- | | | |
| Deferred tax liabilities: | | | |
| Depreciation | \$ 74.3 | \$ 78.6 | \$ 75.4 |
| Other | 2.0 | 10.1 | 12.9 |
| Total deferred tax liabilities | 76.3 | 88.7 | 88.3 |
| ----- | | | |
| Deferred tax assets: | | | |
| Employee benefit plans | 36.5 | 23.8 | 19.8 |
| Doubtful accounts | 9.7 | 6.7 | 5.1 |
| Inventories | 5.0 | 5.4 | 5.6 |
| Amortization of intangibles | 22.8 | 24.4 | 15.1 |
| Accruals | 18.3 | 18.6 | 18.0 |
| Restructuring charges | 71.1 | 15.1 | 19.2 |
| Other | - | 6.1 | 1.7 |
| Total deferred tax assets | 163.4 | 100.1 | 84.5 |
| ----- | | | |
| Net deferred tax assets (liabilities) | \$ 87.1 | \$ 11.4 | \$ (3.8) |
| ----- | | | |

Income tax expense consisted of the following:

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|--------------------------|---------|---------|---------|
| ----- | | | |
| Current: | | | |
| Federal | \$48.5 | \$ 49.4 | \$ 26.0 |
| Foreign | 28.7 | 19.5 | 21.1 |
| State | 8.8 | 12.6 | 7.5 |
| Total current | 86.0 | 81.5 | 54.6 |
| ----- | | | |
| Deferred (benefit): | | | |
| Federal | (36.9) | 2.0 | 1.2 |
| Foreign | (21.6) | (3.7) | .3 |
| State | (4.2) | (2.5) | (2.4) |
| Total deferred (benefit) | (62.7) | (4.2) | (0.9) |
| ----- | | | |
| Total | \$ 23.3 | \$ 77.3 | \$ 53.7 |
| ----- | | | |

Income taxes paid during 1997, 1996 and 1995 were \$69.1 million, \$64.4 million and \$74.1 million, respectively.

The reconciliation of the federal income tax at the statutory federal rate to the income tax at the effective rate was as follows:

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|---|----------|---------|---------|
| ----- | | | |
| Tax at statutory rate | \$ (6.5) | \$ 61.0 | \$ 39.5 |
| State income taxes, net of federal benefits | 3.8 | 6.9 | 5.5 |
| Difference between foreign and federal income tax | 1.9 | .7 | 1.4 |
| Restructuring reserves | 24.3 | 7.1 | 8.0 |
| Other-net | (.2) | 1.6 | (.7) |
| ----- | | | |
| Income taxes | \$ 23.3 | \$ 77.3 | \$ 53.7 |
| ----- | | | |

The components of earnings (loss) before income taxes consisted of the following:

| (Millions of Dollars) | 1997 | 1996 | 1995 |
|------------------------------|----------|----------|----------|
| ----- | | | |
| United States | \$ 11.1 | \$ 156.6 | \$ 78.5 |
| Foreign | (29.7) | 17.6 | 34.3 |
| ----- | | | |
| Total pretax earnings (loss) | \$(18.6) | \$ 174.2 | \$ 112.8 |

Undistributed foreign earnings of \$169.5 million at January 3, 1998 are considered to be invested indefinitely or will be remitted substantially free of additional tax. Accordingly, no provision has been made for taxes that might be payable upon remittance of such earnings, nor is it practicable to determine the amount of this liability.

P. LEASES

The company leases certain facilities, vehicles, machinery and equipment under long-term operating leases with varying terms and expiration dates.

Future minimum lease payments under noncancelable operating leases, in millions of dollars, as of January 3, 1998 were \$22.4 in 1998, \$18.3 in 1999, \$15.2 in 2000, \$11.1 in 2001, \$7.3 in 2002 and \$29.5 thereafter. Minimum payments have not been reduced by minimum sublease rentals of \$15.7 million due in the future under noncancelable subleases. Rental expense for operating leases amounted to \$34.9 million in 1997, \$36.6 million in 1996 and \$40.3 million in 1995.

Q. CONTINGENCIES

In the normal course of business, the company is involved in various lawsuits and claims. In addition, the company is a party to a number of proceedings before federal and state regulatory agencies relating to environmental remediation. Also, the company, along with many other companies, has been named as a potentially responsible party (PRP) in a number of administrative proceedings for the remediation of various waste sites, including nine Superfund sites. Current laws potentially impose joint and several liability upon each PRP. In assessing its potential liability at these sites, the company has considered the following: the solvency of the other PRPs, whether responsibility is being disputed, the terms of existing agreements, experience at similar sites, and the fact that the company's volumetric contribution at these sites is relatively small.

The company's policy is to accrue environmental investigatory and remediation costs for identified sites when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The amount of liability recorded is based on an evaluation of currently available facts with respect to each individual site and includes such factors as existing technology, presently enacted laws and regulations, and prior experience in remediation of contaminated sites. The liabilities recorded do not take into account any claims for recoveries from insurance or third parties. As assessments and remediation progress at individual sites, the amounts recorded are reviewed periodically and adjusted to reflect additional technical and legal information that becomes available. As of January 3, 1998, the company had reserves of \$31.9 million, primarily for remediation activities associated with company-owned properties as well as for Superfund sites.

The amount recorded for identified contingent liabilities is based on estimates. Amounts recorded are reviewed periodically and adjusted to reflect additional technical and legal information that becomes available. Actual costs to be incurred in future periods may vary from the estimates, given the inherent uncertainties in evaluating certain exposures. Subject to the imprecision in estimating future contingent liability costs, the company does not expect that any sum it may have to pay in connection with these matters in excess of the amounts recorded will have a materially adverse effect on its financial position, results of operations or liquidity.

QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

(Millions of Dollars, except per share amounts)

| | Quarter | | | | Year |
|--|----------|-----------|-----------|----------|-----------|
| | First | Second | Third | Fourth | |
| 1997 | | | | | |
| Net sales | \$ 646.6 | \$ 673.6 | \$ 650.5 | \$ 698.8 | \$2,669.5 |
| Gross profit | 215.2 | 227.5 | 213.9 | 229.5 | 886.1 |
| Selling, general and administrative expenses | 153.2 | 153.8 | 148.2 | 172.5 | 627.7 |
| Restructuring and asset write-offs | (4.6) | 137.2 | 105.9 | - | 238.5 |
| Net earnings (loss) | \$ 36.7 | \$ (64.5) | \$ (40.6) | \$ 26.5 | \$ (41.9) |
| Net earnings (loss) per share: | | | | | |
| Basic | \$.41 | \$ (.72) | \$ (.46) | \$.30 | \$ (.47) |
| Diluted | \$.41 | \$ (.72) | \$ (.46) | \$.29 | \$ (.47) |
| 1996 | | | | | |
| Net sales | \$ 635.3 | \$ 677.2 | \$ 672.9 | \$ 685.4 | \$2,670.8 |
| Gross profit | 206.0 | 224.2 | 224.5 | 220.6 | 875.3 |
| Selling, general and administrative expenses | 149.0 | 153.1 | 151.7 | 154.7 | 608.5 |
| Restructuring and asset write-offs | - | 3.8 | 3.1 | 40.9 | 47.8 |
| Net earnings (loss) | \$ 29.6 | \$ 32.6 | \$ 37.7 | \$ (3.0) | \$ 96.9 |
| Net earnings (loss) per share: | | | | | |
| Basic | \$.33 | \$.37 | \$.42 | \$ (.03) | \$ 1.09 |
| Diluted | \$.33 | \$.36 | \$.42 | \$ (.03) | \$ 1.08 |

Note: The second quarter of 1997 includes a charge of \$10.6 million, or \$.07 per share, for a stock option grant as specified in the company's employment contract with its chief executive officer. The fourth quarter of 1996 includes a charge of \$7.6 million, or \$.08 per share, for other elements of this contract.

CORPORATE INFORMATION

BOARD OF DIRECTORS

John M. Trani 1
Chairman and
Chief Executive Officer
The Stanley Works

Mannie L. Jackson 2, 5
Chairman
Harlem Globetrotters International, a division of MJA, Inc.

Hugo E. Uytterhoeven 3, 4
Professor, Graduate School
of Business Administration
Harvard University

Stillman B. Brown 1, 4, 5
Managing General Partner Harcott Associates
Investments

James G. Kaiser 2, 5
Retired; former President
and Chief Executive Officer Quanterra Incorporated,
a subsidiary of Corning Incorporated and
International Technology Inc.

Walter W. Williams 3, 5
Retired; former Chairman
and Chief Executive Officer
Rubbermaid, Incorporated

Edgar R. Fiedler 3, 4
Retired; former
Vice President and
Economic Counselor
The Conference Board

Eileen S. Kraus 1, 2, 4
Chairman, Connecticut
Fleet National Bank

Kathryn D. Wriston 1, 2, 3
Director of various
organizations

CORPORATE OFFICERS

JOHN A. COSENTINO, JR.
Vice President, Operations
(1997)

WILLIAM D. HILL
Vice President, Engineering and Technology
(1997)

KENNETH O. LEWIS
Vice President, Marketing and Brand Development
(1997)

MARK J. MATHIEU
Vice President, Human Resources
(1997)

THOMAS E. MAHONEY
President, Consumer Sales Americas
(1965)

PAUL W. RUSSO
Vice President, Strategy and Development
(1995)

JOHN M. TRANI
Chairman and Chief Executive Officer
(1997)

STEPHEN S. WEDDLE
Vice President, General Counsel and Secretary
(1978)

THERESA F. YERKES
Vice President and Controller
(1989)

(Joined Stanley)

- 1 Member of the Executive Committee
- 2 Member of the Audit Committee
- 3 Member of the Board Affairs and Public Policy Committee
- 4 Member of the Finance and Pension Committee
- 5 Member of the Compensation and Organization Committee

INVESTOR AND SHAREOWNER INFORMATION

COMMON STOCK

The Stanley Works common stock is listed on the New York and Pacific Stock Exchanges under the abbreviated ticker symbol "SWK."

Stock (Dollars per Share)

| | Price | | | | Dividends | | |
|----------------|---------|----------|----------|--------|-----------|--------|-------|
| | 1997 | | 1996 | | 1997 | 1996 | |
| | High | Low | High | Low | | | |
| First Quarter | 41 | 28 | 28 | 5/8 | 24 1/16 | \$.185 | \$.18 |
| Second Quarter | 44 3/8 | 35 1/2 | 32 13/16 | 27 1/8 | | .185 | .18 |
| Third Quarter | 47 3/8 | 39 1/4 | 30 3/4 | 23 5/8 | | .20 | .185 |
| Fourth Quarter | 47 3/16 | 39 15/16 | 30 1/2 | 26 3/8 | | .20 | .185 |
| | | | | | | \$.77 | \$.73 |

DIVIDENDS

The Stanley Works has an impressive and truly unique dividend record over the long haul:

- o Our record of annual dividend payments is unmatched by any industrial company listed on the New York Stock Exchange-- 121 consecutive years.
- o Our quarterly dividend record is the longest of any industrial company listed on the New York Stock Exchange-- 411 consecutive quarters.
- o We have increased dividends in each of the past 30 years, and in that same period, an investment in Stanley stock grew at a compound annual rate of 14.4%.

INCREASED DIVIDENDS EVERY YEAR SINCE 1968

Dividend per share in Dollars \$.77 per share

[GRAPHIC LINE CHART SHOWING INCREASED DIVIDENDS EVERY YEAR SINCE 1968]

TRANSFER AGENT AND REGISTRAR

All shareowner inquiries, including transfer-related matters, should be directed to:

Boston EquiServe, Servicing Agent for
State Street Bank and Trust Company
P.O. Box 8200
Boston, MA 02266-8200
800-426-5523

CORPORATE OFFICES

The company's principal corporate offices are located at:

1000 Stanley Drive, New Britain,
Connecticut 06053.
Telephone 860-225-5111.

ANNUAL MEETING

The annual shareowners' meeting of The Stanley Works will be held at 9:30 a.m. on Wednesday, April 15, 1998, in New Britain, Connecticut at the Stanley Center, 1255 Corbin Avenue. A formal notice of the meeting together with a proxy statement has been mailed to shareowners with this annual report.

INDEPENDENT AUDITORS

Ernst & Young LLP, 225 Asylum Street,
Hartford, Connecticut 06103

FINANCIAL & INVESTOR COMMUNICATIONS

The Stanley Works investor relations department provides information to shareowners and the financial community. We encourage inquiries and will provide services which include:

- o fulfilling requests for annual reports, proxy statements, form 10-Q, form 10-K, copies of press releases and other company information.
- o meetings with securities analysts and fund managers.

Contact The Stanley Works investor relations department at our corporate offices by calling Gerard J. Gould, Director, Investor Relations at (860) 827-3833. We make quarterly news releases available on-line on the Internet on the day that results are released to the news media. The Stanley Works releases

will be found at the following address on the World Wide Web:
<http://www.prnewswire.com>. Click on "Company News On-Call." Shareowners may also visit our Internet home page at: <http://www.stanleyworks.com>. Stanley shareowners are also able to call toll-free 800-499-9202 to request a copy of the most recent quarterly release.

[PHOTOGRAPH OF JOHN M. TRANI AND THE DIRECTORS AT THE NEW YORK STOCK EXCHANGE]

In recognition of Stanley's outstanding dividend record, including its 30th consecutive annual dividend increase, the New York Stock Exchange invited John M. Trani, Chairman and Chief Executive Officer, to ring the opening bell on July 18, 1997.

Use of (R) or (TM) in this annual report indicates trademarks owned by The Stanley Works and its subsidiaries except that Coca-Cola(R) is a registered trademark of the Coca-Cola Company.

EXHIBIT 21

(All subsidiaries are included in the Consolidated Financial Statements of The Stanley Works)

| Corporate Name ----- | Jurisdiction of Incorporation ----- |
|---------------------------------------|---|
| The Stanley Works | Connecticut |
| The Farmington River Power Company | Connecticut |
| Stanley Germany Inc. | Delaware |
| Stanley International Sales, Inc. | Delaware |
| Stanley Foreign Sales Corporation | Virgin Islands |
| Stanley Home Automation, Inc. | Delaware |
| Stanley Real Estate Holdings Corp. | Florida |
| Jensen Tools, Inc. | Delaware |
| Stanley-Bostitch, Inc. | Delaware |
| Stanley-Bostitch Holding Corporation | Delaware |
| The Stanley Works Funding Corporation | Delaware |
| Stanley Mail Media, Inc. | Delaware |
| Stanley Logistics, Inc. | Delaware |
| Stanley Fastening Systems, L.P. | Delaware |
| Stanley Receivables Corp. | Delaware |
| Stanley European Holdings, L.L.C. | Delaware |
| Stanley Canada Inc. | Ontario, Canada |
| Stanley Tools (N.Z.) Ltd. | New Zealand |
| Ferramentas Stanley Ltda. | Brazil |
| Herramientas Stanley S.A. de C.V. | Mexico |
| Stanley-Bostitch, S.A. de C.V. | Mexico |
| Stanley Tools SpA | Italy |

EXHIBIT 21

| Corporate Name ----- | Jurisdiction of Incorporation ----- |
|--|---|
| (The Stanley Works) | |
| Stanley Atlantic, Inc. | Delaware |
| The Stanley Works Ltd. | U.K. |
| Mosley-Stone Ltd. | U.K. |
| R.J. Lendrum Limited | U.K. |
| Stanley Works (Nederland) B.V. | Netherlands |
| Stanley Magic-Door Netherlands B.V. | Netherlands |
| Placements et Rangements Nirva S.a.R.L. | France |
| S.I.C.F.O.-Stanley S.A. | France |
| Stanley Bostitch S.A. | France |
| Soc. de Fab. Bostitch S.A.(Simax) | France |
| Societe Civile Immobiliere WAT | France |
| Stanley Iberica S.A. | Spain |
| Stanley Vaerktoej ApS | Denmark |
| Stanley Svenska A.B. | Sweden |
| Suomen Stanley OY | Finland |
| Bostitch G.m.b.H. | Germany |
| Friess G.m.b.H. | Germany |
| Bostitch (Europe) AG | Switzerland |
| Bostitch AG | Switzerland |
| S.A. Stanley Works Belgium N.V. | Belgium |
| The Stanley Works C.V. | Netherlands |

EXHIBIT 21

| Corporate Name ----- | Jurisdiction of Incorporation ----- |
|--|---|
| (The Stanley Works) | |
| Stanley International Holdings Inc. | Delaware |
| Stanley Pacific Inc. | Delaware |
| Stanley-Bostitch Pty. Limited | Australia |
| The Stanley Works Pty. Ltd. | Australia |
| Stanley Works Asia Pacific Pte. Ltd. | Singapore |
| The Stanley Works (Hong Kong) Ltd. | Hong Kong |
| The Stanley Works Sales (Philippines), Inc. | Philippines |
| Stanley Tools Ltd. | Taiwan |
| Chiro Tool Manufacturing Corporation | Taiwan |
| The Stanley Works (Bermuda) Ltd. | Bermuda |
| The Stanley Works Japan K.K. | Japan |
| Stanley Works Ltd. | Thailand |
| Stanley Tools Poland Ltd. | Poland |
| Tona a.s. (LTD) (86%) | Czech Republic |
| P.T. Stanley Works Indonesia | Indonesia |
| Stanley Works Malaysia Sdn. Bhd. | Malaysia |
| Stanley Fastening Systems Poland Ltd. | Poland |
| Stanley de Chihuahua, S. de R.L. de C.V. | Mexico |
| Stanley Works China Investments Ltd. (65%) | Virgin Islands |
| Stanley (Zhongshan) Hardware Co. Ltd. (65%) | China |
| Stanley U.K. Holding Limited | U.K. |

EXHIBIT 21

| Corporate Name ----- | Jurisdiction of Incorporation ----- |
|---|---|
| (The Stanley Works) | |
| Stanley Chiro International Ltd. | Taiwan |
| Stanley Italia S.r.l. | Italy |
| ATRO Ltd. | U.K. |
| DIMAC S.a.r.l. | France |
| International Staple & Machine Co. n.v. | Belgium |
| FIPADUE S.r.l. | Italy |
| Beijing Daxing Stanley-Bostitch Metal Industries Company Limited (98%) | China |

The names of certain subsidiaries have been omitted because such subsidiaries, considered in the aggregate as a single subsidiary, would not constitute a significant subsidiary.

This schedule contains summary financial information extracted from The Stanley Works and Subsidiaries Consolidated Balance Sheets and Statements of Operations and is qualified in its entirety by reference to such financial statements.

1,000

| YEAR | |
|-------------|-----------|
| JAN-03-1998 | |
| JAN-03-1998 | 152,200 |
| | 0 |
| | 429,300 |
| | 19,800 |
| | 301,200 |
| 1,005,300 | |
| | 1,166,100 |
| | 652,900 |
| 1,758,700 | |
| 622,700 | |
| | 283,700 |
| 0 | |
| | 0 |
| | 230,900 |
| 1,758,700 | |
| | 376,900 |
| | 2,669,500 |
| 2,669,500 | |
| | 1,783,400 |
| 1,783,400 | |
| | 0 |
| | 0 |
| 16,600 | |
| (18,600) | |
| | 23,300 |
| (41,900) | |
| | 0 |
| | 0 |
| | 0 |
| | (41,900) |
| | (.47) |
| | (.47) |

THE STANLEY WORKS AND SUBSIDIARIES
RESTATED FINANCIAL DATA SCHEDULE

This schedule contains summary financial information extracted from The Stanley Works and Subsidiaries Consolidated Balance Sheets and Statements of Operations and is qualified in its entirety by reference to such financial statements.

1,000

| 9-MOS | 6-MOS | | 3-MOS | | YEAR | |
|-----------|----------------------------|----------------------------|----------------------------|----------------------------|----------------------------|----------------------------|
| | JAN-03-1998 SEP-27-1997 | JAN-03-1998 JUN-28-1997 | JAN-03-1998 JUN-28-1997 | JAN-03-1998 MAR-29-1997 | DEC-28-1996 DEC-28-1996 | DEC-28-1996 DEC-28-1996 |
| | 146,700 | 107,600 | | 76,400 | | 84,000 |
| | 0 | 0 | | 0 | | 0 |
| | 483,200 | 457,100 | | 453,300 | | 468,800 |
| | 0 | 0 | | 0 | | 22,500 |
| | 307,700 | 323,400 | | 329,200 | | 338,100 |
| | 1,018,200 | 940,900 | | 899,200 | | 910,900 |
| | 1,159,900 | 1,160,300 | | 1,206,300 | | 1,224,400 |
| | 656,700 | 652,000 | | 644,700 | | 654,000 |
| | 1,736,600 | 1,666,800 | | 1,633,500 | | 1,659,600 |
| | 575,700 | 490,200 | | 387,000 | | 381,600 |
| | 288,900 | 295,800 | | 298,900 | | 342,600 |
| | 0 | 0 | | 0 | | 0 |
| | 0 | 0 | | 0 | | 0 |
| | 230,900 | 230,900 | | 230,900 | | 230,900 |
| | 409,200 | 485,800 | | 561,000 | | 549,200 |
| 1,736,600 | 1,666,800 | 1,633,500 | | 1,659,600 | | 2,670,800 |
| | 1,970,700 | 1,320,200 | | 646,600 | | 2,670,800 |
| | 1,314,100 | 877,500 | | 431,400 | | 1,795,500 |
| | 0 | 0 | | 0 | | 0 |
| | 0 | 0 | | 0 | | 0 |
| | 12,900 | 8,700 | | 4,300 | | 22,500 |
| | (69,200) | (22,800) | | 58,700 | | 174,200 |
| | (800) | 5,000 | | 22,000 | | 77,300 |
| (68,400) | (27,800) | | | 36,700 | | 96,900 |
| | 0 | 0 | | 0 | | 0 |
| | 0 | 0 | | 0 | | 0 |
| | 0 | 0 | | 0 | | 0 |
| | (68,400) | (27,800) | | 36,700 | | 96,900 |
| | (.77) | (.31) | | .41 | | 1.09 |
| | (.77) | (.31) | | .41 | | 1.08 |

In December 1997, the company adopted Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share". All per share data on the above Financial Data Schedule has been retroactively restated in accordance with SFAS No. 128.

This schedule contains summary financial information extracted from The Stanley Works and Subsidiaries Consolidated Balance Sheets and Statements of Operations and is qualified in its entirety by reference to such financial statements.

1,000

| 9-MOS | 6-MOS | | 3-MOS | | YEAR | |
|-----------|----------------------------|----------------------------|----------------------------|----------------------------|----------------------------|----------------------------|
| | DEC-28-1996 SEP-28-1996 | DEC-28-1996 JUN-29-1996 | DEC-28-1996 JUN-29-1996 | DEC-28-1996 MAR-30-1996 | DEC-30-1995 DEC-30-1995 | DEC-30-1995 DEC-30-1995 |
| | 85,000 | 79,500 | 79,500 | 39,300 | 75,400 | 75,400 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 473,800 | 454,200 | 454,200 | 454,900 | 456,900 | 456,900 |
| | 0 | 0 | 0 | 0 | 18,200 | 18,200 |
| | 342,400 | 344,400 | 344,400 | 335,200 | 349,100 | 349,100 |
| | 941,000 | 920,400 | 920,400 | 875,200 | 915,100 | 915,100 |
| | 1,219,100 | 1,202,000 | 1,202,000 | 1,196,400 | 1,186,200 | 1,186,200 |
| | 656,500 | 646,000 | 646,000 | 641,700 | 629,700 | 629,700 |
| | 1,689,600 | 1,668,600 | 1,668,600 | 1,628,400 | 1,670,000 | 1,670,000 |
| 397,300 | | 371,400 | | 348,400 | 387,700 | 387,700 |
| | 350,600 | 373,300 | 373,300 | 384,000 | 391,100 | 391,100 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 230,900 | 230,900 | 230,900 | 230,800 | 115,400 | 115,400 |
| | 556,800 | 534,800 | 534,800 | 512,500 | 619,200 | 619,200 |
| 1,689,600 | 1,668,600 | 1,628,400 | 1,628,400 | 1,670,000 | 2,624,300 | 2,624,300 |
| | 1,985,400 | 1,312,500 | 1,312,500 | 635,300 | 2,624,300 | 2,624,300 |
| | 1,330,700 | 882,300 | 882,300 | 429,300 | 1,789,700 | 1,789,700 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 17,100 | 11,900 | 11,900 | 6,500 | 30,300 | 30,300 |
| | 163,500 | 104,500 | 104,500 | 47,000 | 112,800 | 112,800 |
| | 63,600 | 42,300 | 42,300 | 17,400 | 53,700 | 53,700 |
| 99,900 | | 62,200 | | 29,600 | 59,100 | 59,100 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 0 | 0 | 0 | 0 | 0 |
| | 99,900 | 62,200 | 62,200 | 29,600 | 59,100 | 59,100 |
| | 1.12 | .70 | .70 | .33 | .66 | .66 |
| | 1.11 | .69 | .69 | .33 | .66 | .66 |

In December 1997, the company adopted Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share". All per share data on the above Financial Data Schedule has been retroactively restated in accordance with SFAS No. 128.

AUDITED FINANCIAL STATEMENTS
AND SUPPLEMENTAL SCHEDULES

THE STANLEY WORKS 401(k) SAVINGS PLAN

Years ended December 31, 1997 and 1996

The Stanley Works 401(k) Savings Plan

Audited Financial Statements
and Supplemental Schedules

Years ended December 31, 1997 and 1996

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Report of Independent Auditors

Pension Committee of The Board of Directors
The Stanley Works

We have audited the accompanying statements of financial condition of The Stanley Works 401(k) Savings Plan as of December 31, 1997 and 1996, and the related statements of income and changes in plan equity for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial condition of the Plan at December 31, 1997 and 1996, and its income and changes in plan equity for the years then ended in conformity with generally accepted accounting principles.

Our audits were performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplemental schedules of assets held for investment as of December 31, 1997, and transactions or series of transactions in excess of 5% of the current value of plan assets for the year then ended, are presented for purposes of complying with the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974, and are not a required part of the financial statements. The supplemental schedules have been subjected to the auditing procedures applied in our audit of the 1997 financial statements and, in our opinion, are fairly stated in all material respects in relation to the 1997 financial statements taken as a whole.

Ernst & Young LLP

Hartford, Connecticut
March 13, 1998

The Stanley Works 401(k) Savings Plan

Statement of Financial Condition

December 31, 1997

| | STANLEY STOCK FUND | LOAN FUND | UNALLOCATED STANLEY STOCK FUND | TOTAL |
|--|-----------------------|---------------|--------------------------------------|---------------------------|
| ASSETS | | | | |
| Investments, at current market value: | | | | |
| The Stanley Works | | | | |
| Common Stock: | | | | |
| 8,997,264 shares (cost \$132,445,673) | \$424,558,395 | | | \$424,558,395 |
| 10,007,568 shares (cost \$181,101,634) | | | \$472,232,116 | 472,232,116 |
| Short-term investments | 2,515,153 | | | 2,515,153 |
| | 427,073,548 | | 472,232,116 | 899,305,664 |
| Contributions receivable | 3,062,065 | | | 3,062,065 |
| Dividends and interest receivable | 45,195 | | 1,594,244 | 1,639,439 |
| Loans to participants | | \$ 12,323,967 | | 12,323,967 |
| | \$430,180,808 | \$ 12,323,967 | \$473,826,360 | \$916,331,135 |
| LIABILITIES AND PLAN EQUITY | | | | |
| Liabilities: | | | | |
| Due to Retirement Plan for Salaried Employees of The Stanley Works | | | | |
| Debt | \$ 262,146 | | \$224,647,020 | \$ 262,146 224,647,020 |
| | 262,146 | | 224,647,020 | 224,909,166 |
| Plan equity | 429,918,662 | \$ 12,323,967 | 249,179,340 | 691,421,969 |
| | \$430,180,808 | \$ 12,323,967 | \$473,826,360 | \$916,331,135 |

See accompanying notes.

The Stanley Works 401(k) Savings Plan

Statement of Financial Condition

December 31, 1996

| | STANLEY STOCK FUND | LOAN FUND | UNALLOCATED STANLEY STOCK FUND | TOTAL |
|--|-----------------------|--------------|--------------------------------------|---------------|
| | ----- | | | |
| ASSETS | | | | |
| Investments, at current market value: | | | | |
| The Stanley Works Common Stock: | | | | |
| 9,449,808 shares (cost \$137,198,542) | \$255,144,816 | | | \$255,144,816 |
| 10,800,908 shares (cost \$194,540,603) | | | \$291,624,516 | 291,624,516 |
| Short-term investments | 4,089,979 | | 284,230 | 4,374,209 |
| | ----- | | ----- | ----- |
| | 259,234,795 | | 291,908,746 | 551,143,541 |
| Dividends and interest receivable | 7,557 | | 1,240 | 8,797 |
| Loans to participants | | \$11,495,638 | | 11,495,638 |
| | ----- | ----- | ----- | ----- |
| | \$259,242,352 | \$11,495,638 | \$291,909,986 | \$562,647,976 |
| | ===== | ===== | ===== | ===== |
| LIABILITIES AND PLAN EQUITY | | | | |
| Liabilities: | | | | |
| Due to Retirement Plan for Salaried Employees of The Stanley Works | \$ 262,146 | | | \$ 262,146 |
| Debt | | | \$234,789,748 | 234,789,748 |
| | ----- | | ----- | ----- |
| | 262,146 | | 234,789,748 | 235,051,894 |
| Plan equity | 258,980,206 | \$11,495,638 | 57,120,238 | 327,596,082 |
| | ----- | ----- | ----- | ----- |
| | \$259,242,352 | \$11,495,638 | \$291,909,986 | \$562,647,976 |
| | ===== | ===== | ===== | ===== |

See accompanying notes.

The Stanley Works 401(k) Savings Plan
Statement of Income and Changes in Plan Equity
Year ended December 31, 1997

| | STANLEY STOCK FUND | LOAN FUND | UNALLOCATED STANLEY STOCK FUND | TOTAL |
|--|-----------------------|--------------|--------------------------------------|---------------|
| | | | | |
| Investment income: | | | | |
| Dividends | \$ 7,197,351 | | \$ 7,993,754 | \$ 15,191,105 |
| Interest | 91,621 | \$ 881,528 | 15,600 | 988,749 |
| | 7,288,972 | 881,528 | 8,009,354 | 16,179,854 |
| Net realized and unrealized appreciation in The Stanley Works Common Stock | 194,715,441 | | 194,046,566 | 388,762,007 |
| Employee contributions | 20,080,006 | | | 20,080,006 |
| Withdrawals: | | | | |
| Cash | (36,544,886) | | | (36,544,886) |
| The Stanley Works Common Stock | (5,316,015) | | | (5,316,015) |
| | (41,860,901) | | | (41,860,901) |
| Administrative expenses | (537,601) | | (845) | (538,446) |
| Interest expense | | | (18,796,633) | (18,796,633) |
| Interfund transfers - net | (8,747,461) | (53,199) | 8,800,660 | |
| | 170,938,456 | 828,329 | 192,059,102 | 363,825,887 |
| Plan equity at beginning of year | 258,980,206 | 11,495,638 | 57,120,238 | 327,596,082 |
| Plan equity at end of year | \$429,918,662 | \$12,323,967 | \$249,179,340 | \$691,421,969 |
| | ===== | ===== | ===== | ===== |

See accompanying notes.

The Stanley Works 401(k) Savings Plan
Statement of Income and Changes in Plan Equity
Year ended December 31, 1996

| | STANLEY STOCK FUND | LOAN FUND | UNALLOCATED STANLEY STOCK FUND | TOTAL |
|--|-----------------------|--------------|--------------------------------------|---------------|
| | | | | |
| Investment income: | | | | |
| Dividends | \$ 6,909,565 | | \$ 8,160,284 | \$ 15,069,849 |
| Interest | 93,635 | \$ 680,930 | 6,224 | 780,789 |
| | 7,003,200 | 680,930 | 8,166,508 | 15,850,638 |
| Net realized and unrealized appreciation in The Stanley Works Common Stock | 16,422,570 | | 5,764,892 | 22,187,462 |
| Contributions: | | | | |
| Employee | 19,968,699 | | | 19,968,699 |
| Employer | 6,232,568 | | | 6,232,568 |
| | 26,201,267 | | | 26,201,267 |
| Withdrawals: | | | | |
| Cash | (34,756,301) | | | (34,756,301) |
| The Stanley Works Common Stock | (4,783,322) | | | (4,783,322) |
| | (39,539,623) | | | (39,539,623) |
| Administrative expenses | (435,997) | | | (435,997) |
| Interest expense | | | (19,550,376) | (19,550,376) |
| Interfund transfers - net | (3,775,570) | (857,031) | 4,632,601 | |
| | 5,875,847 | (176,101) | (986,375) | 4,713,371 |
| Net increase (decrease) | | | | |
| Plan equity at beginning of year | 253,104,359 | 11,671,739 | 58,106,613 | 322,882,711 |
| Plan equity at end of year | \$258,980,206 | \$11,495,638 | \$ 57,120,238 | \$327,596,082 |

See accompanying notes.

The Stanley Works 401(k) Savings Plan

Notes to Financial Statements

December 31, 1997

1. DESCRIPTION OF THE PLAN

The Stanley Works 401(k) Savings Plan (the "Savings Plan") operates as a leveraged employee stock ownership plan, is designed to comply with the Internal Revenue Code of 1986, as amended, and is subject to the applicable provisions of the Employee Retirement Income Security Act of 1974, as amended. The Savings Plan is a defined contribution plan for eligible United States salaried and hourly paid employees of The Stanley Works (the "Company").

Each year, participants may contribute, through pre-tax payroll deductions up to 15% of their compensation, as defined in the Savings Plan Agreement. Such contributions are matched by the Company in an amount equal to 50% of the participant's contribution up to a maximum matching contribution of 3 1/2% of the participant's compensation.

Participant and Company contributions are invested in the Stanley Stock Fund with a guarantee, which, if necessary, is satisfied by the Retirement Plan for Salaried Employees of The Stanley Works or by the Pension Plan for Hourly Paid Employees of The Stanley Works, that the investment return on such stock acquired with employee contributions will not be less than an investment return based on two-year U.S. Treasury notes.

Employees are fully vested as to amounts in their savings accounts attributable to their own contributions and earnings thereon and amounts transferred from the other qualified plans on their behalf. All participants are vested in 100% of the value of the Company matching contributions made on their behalf after five years of service, with no vesting in the matching contributions during the first through fifth years of service.

The assets of the Savings Plan are held in trust by an independent corporate trustee, State Street Bank and Trust Company (the "Trustee") pursuant to the terms of a written Trust Agreement between the Trustee and the Company.

Benefits generally are distributed upon termination of employment. Normally, a lump-sum distribution is made in cash or shares of the Company's Common Stock (hereinafter referred to as Common Stock, Stanley Stock, or shares), at the election of the participant, from the Stanley Stock Fund.

During active employment, subject to financial hardship rules, participants may withdraw, in cash only, all or a portion of vested amounts in their accounts.

The Stanley Works 401(k) Savings Plan
Notes to Financial Statements (continued)

1. DESCRIPTION OF THE PLAN (CONTINUED)

Participants may borrow from their savings account up to an aggregate amount equal to the lesser of \$50,000 or 50% of the value of their vested interest in such accounts with a minimum loan of \$1,000. The \$50,000 loan amount limitation is reduced by the participant's highest outstanding loan balance during the 12 months preceding the date the loan is made. Each loan is evidenced by a negotiable promissory note bearing a rate of interest equal to the prime rate as reported in The Wall Street Journal on the first business day of the month immediately preceding the calendar quarter during which the loan was made, which is payable, through payroll deductions, over a term of not more than five years. Participants are allowed ten years to repay the loan if the proceeds are used to purchase a principal residence. Only one loan per participant may be outstanding at any time.

If a loan is outstanding at the time a distribution becomes payable to a participant (or beneficiary), the distribution is made net of the loan outstanding, and the distribution shall fully discharge the Savings Plan with respect to the participant's account value attributable to the outstanding loan balance.

The Savings Plan borrowed \$95,000,000 in 1989 from a group of financial institutions and \$180,000,000 in 1991 from the Company (see Notes 3 and 4) to acquire 5,868,088 and 9,696,968 shares, respectively, of Common Stock from the Company's treasury and previously unissued shares. The shares purchased from the proceeds of the loans were placed in the Unallocated Stanley Stock Fund (the "Unallocated Fund"). Under the 1989 loan agreement, the Company guaranteed the loan and is obligated to make annual contributions sufficient to enable the Plan to repay the loan plus interest.

The Unallocated Fund makes monthly transfers of shares, in accordance with The Savings Plan provisions, to the Stanley Stock Fund in return for proceeds equivalent to the average fair market value of the shares for the month subsequent to the last transfer. These proceeds, along with dividends received on allocated and unallocated shares and additional employee and Company contributions, if necessary, are used to make monthly payments of principal and interest on the debt. As dividends on the allocated shares are applied to the payment of debt service, a number of shares having a fair market value at least equal to the amount of the dividends so applied are allocated to the savings accounts of participants who would otherwise have received cash dividends. The excess of unallocated dividends over the amount necessary for principal and interest along with forfeitures of nonvested employee accounts are used to reduce future Company matching contributions. During 1997, these excess funds fully offset the Company's matching contribution.

The Stanley Works 401(k) Savings Plan
Notes to Financial Statements (continued)

1. DESCRIPTION OF THE PLAN (CONTINUED)

The fair market value of shares released from the Unallocated Fund pursuant to loan repayments made during any year may exceed the total of employee contributions and Company matching contributions for that year. If that occurs, all participants who made contributions at any time during that year and who are employed by the Company on the last day of that year receive, on a pro rata basis, such excess value as an additional allocation of Stanley Stock for that year.

Each participant is entitled to exercise voting rights attributable to the shares allocated to their account. The Trustee is not permitted to vote participant shares for which instructions have not been given by the participant. Shares in the Unallocated Fund are voted by the Trustee in the same proportion as allocated shares.

The Company reserves the right to terminate the Savings Plan at any time, subject to its provisions. Upon such termination of the Savings Plan, the interest of each participant in the trust fund will become vested and be distributed to such participant or his or her beneficiary at the time prescribed by the Savings Plan terms and the Internal Revenue Code.

The Savings Plan sponsor has engaged William Mercer, Inc., to maintain separate accounts for each participant. Such accounts are credited with each participant's contributions, the allocated portion of the Company's matching contributions, related gains, losses and dividend income, and loan activity.

There were 10,501 and 10,805 participants (9,612 and 10,131 of whom were active employees) in the plan as of December 31, 1997 and 1996, respectively, of whom 2,324 and 2,537, respectively, had loans outstanding.

At December 31, 1997 and 1996, benefits payable to terminated vested participants amounted to \$6,864,864 and \$1,800,388, respectively.

The Stanley Works 401(k) Savings Plan
Notes to Financial Statements (continued)

2. SIGNIFICANT ACCOUNTING POLICIES

INVESTMENTS

The Savings Plan investments consist primarily of shares of Stanley Stock. Stanley Stock is traded on a national exchange and is valued at the last reported sales price on the last business day of the plan year. On April 17, 1996, the Board of Directors of the Company declared a two-for-one common stock split. All share amounts have been restated to reflect the stock split. Short-term investments consist of short-term bank-administered trust funds which earn interest daily at rates approximating U.S. Government securities; cost approximates market value.

DIVIDEND INCOME

Dividend income is accrued on the ex-dividend date.

GAINS OR LOSSES ON SALES OF INVESTMENTS

Gains or losses realized on the sales of investments are determined based on average cost.

EXPENSES

Administrative expenses not paid by the Company are paid by the Savings Plan.

3. DEBT

Debt consisted of the following at December 31:

| | 1997 | 1996 |
|--|---------------|---------------|
| | ---- | ---- |
| Notes payable in monthly installments to 2001 with interest at 7.71% | \$ 47,352,052 | \$ 57,488,780 |
| Notes payable to the Company in monthly installments to 2026 with interest at 8.3% | 177,294,968 | 177,300,968 |
| | ----- | ----- |
| | \$224,647,020 | \$234,789,748 |
| | ===== | ===== |

The scheduled maturities of debt for the next five years are as follows:
1998--\$11,067,000; 1999--\$11,994,000; 2000--\$13,000,000; 2001--\$10,433,000;
and 2002--\$1,852,000.

The Stanley Works 401(k) Savings Plan
Notes to Financial Statements (continued)

3. DEBT (CONTINUED)

The notes payable to the Company are secured by shares held in the Unallocated Stock Fund. The number of shares held as security is reduced as shares are released to Stanley Stock Fund pursuant to principal and interest payments. During the year, 254,094 shares were released and at December 31, 1997, 7,972,316 shares are pledged as security.

Payment of the Savings Plan's debt has been guaranteed by the Company. Should the principal and interest due exceed the dividends paid on shares in the Stanley Stock and Unallocated Stock Funds, and employee and Company matching contributions, the Company is responsible for funding such shortfall.

4. TRANSACTIONS WITH PARTIES-IN-INTEREST

Fees paid during 1997 and 1996 for management and other services rendered by parties-in-interest were based on customary and reasonable rates for such services. The majority of such fees were paid by the Savings Plan. Fees incurred and paid by the Savings Plan during 1997 and 1996 were \$538,446 and \$435,997, respectively.

In 1991, the Savings Plan borrowed \$180,000,000 from the Company, the proceeds of which were used to purchase 9,696,968 shares of stock from the Plan. The Savings Plan made \$14,721,703 and \$14,875,901 of principal and interest payments related to such debt in 1997 and 1996, respectively; at December 31, 1997, \$177,294,968 was outstanding on such debt.

5. INCOME TAX STATUS

The Internal Revenue Service has ruled that the Savings Plan and the trust qualify under Sections 401(a) and 401(k) of the Internal Revenue Code (IRC) and are therefore not subject to tax under present income tax law. Once qualified, the Savings Plan is required to operate in accordance with the IRC to maintain its qualification. The Pension Committee is not aware of any course of action or series of events that have occurred that might adversely affect the Savings Plan's qualified status.

The Stanley Works 401(k) Savings Plan

Assets Held for Investment

December 31, 1997

| IDENTITY OF ISSUE, BORROWER, OR SIMILAR PARTY | DESCRIPTION OF INVESTMENT, INCLUDING MATURITY DATE, RATE OF INTEREST, PAR OR MATURITY VALUE | COST | CURRENT VALUE |
|--|--|------------------------|------------------------|
| Common Stock: | | | |
| The Stanley Works* | 19,004,832 shares of Common Stock; par value \$2.50 per share | \$313,547,307 | \$896,790,511 |
| Trust Funds: | | | |
| State Street Bank and Trust Company* (GSTIF) | Short-Term Investment Fund-United States Government securities | 2,513,141 | 2,513,141 |
| State Street Bank and Trust Company* (STIF) | Short-Term Investment Fund-Pooled Bank Fund | 2,012 | 2,012 |
| Loans to participants | Promissory notes at prime rate with maturities of five years or ten years | 12,323,967 | 12,323,967 |
| Total investments | | \$328,386,427 ===== | \$911,629,631 ===== |

* Indicates party-in-interest to the Plan.

The Stanley Works 401(k) Savings Plan

Transactions or Series of Transactions in Excess of 5% of the
Current Value of Plan Assets

Year Ended December 31, 1997

| IDENTITY OF PARTY INVOLVED | PURCHASE DESCRIPTION OF ASSETS | SELLING PRICE | COST OF ASSET | CURRENT VALUE OF ASSET ON TRANSACTION DATE | NET GAIN (LOSS) |
|---|--|---------------|---------------|--|-----------------|
| Category (iii) - Series of transactions in excess of 5 percent of plan assets | | | | | |
| State Street Bank and Trust Company* | Short-Term Investment Fund-United States Government Securities | | \$34,879,685 | \$34,879,685 | |
| State Street Bank and Trust Company* | Short-Term Investment Fund-United States Government Securities | \$36,454,499 | | 36,454,499 | |

There were no category (i), (ii) or (iv) reportable transactions during 1996.

* Indicates party-in-interest to the Plan.