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Stanley Black & Decker, Inc. (SWK)

Q3 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Third Quarter 2024 Stanley Black & Decker Earnings Conference Call. My name is Shannon, and I will be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.

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

Dennis M. Lange
Vice President-Investor Relations, Stanley Black & Decker, Inc.

Thank you, Shannon. Good morning, everyone. And thanks for joining us for Stanley Black & Decker's 2024, third quarter webcast. Here today, in addition to myself, is Don Allan, President and CEO; Chris Nelson, COO, EVP, and President, Tools & Outdoor; and Pat Hallinan, EVP and CFO.

Our earnings release, which was issued earlier this morning, and a supplemental presentation, which we will refer to are available on the IR section of our website. A replay of this morning's webcast will also be available beginning at 11 AM today.

This morning, Don, Chris and Pat will review our 2024 third quarter results and various other matters, followed by a Q&A session. Consistent with prior webcast, we are going to be sticking with just one question per caller. And as we normally do, we'll be making some forward-looking statements during the call based on our current views.

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Such statements are based on assumptions of future events that may not prove to be accurate, and as such, they involve risk and uncertainty. It's therefore possible that the actual results may materially differ from any forward-looking statements that we might make today. We direct you to the cautionary statements in the 8-K that we filed with our press release and our most recent 1934 Act filing.

Additionally, we may also reference non-GAAP financial measures during the call. For applicable reconciliations to the related GAAP financial measure and additional information, please refer to the appendix of the supplemental presentation and the corresponding press release, which are available on our website under the IR section.

I'll now turn the call over to our President and CEO, Don Allan.

Donald Allan, Jr.

President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

Thank you, Dennis, and good morning, everyone. This quarter, our team again delivered gross margin improvements as well as robust cash generation, all as a result of continued solid execution against our operational priorities, and framework we created over two years ago.

As you saw in this morning's release, we remain focused on executing against key areas within our control, our supply chain transformation and initiatives to accelerate share gain.

By executing our strategy, we continue to reshape our cost structure to capture efficiencies across our value chain and fund new growth investments in a slow, choppy market to gain share.

We expect these actions together will further strengthen our powerful brands, accelerate innovation and enhance our in-market activation to position us as a supplier of choice and capture the compelling long-term opportunities in our industries we serve. Our priorities remain consistent as we work towards completing our strategic transformation.

On today's call, you will hear about progress in each of our key areas of focus: gross margin expansion, strong free cash flow generation; and prioritize investments to stimulate sustainable growth and share gain.

First, gross margin, we continue to drive profitability through the significant transformation of our supply chain to achieve our target of 35-plus percent gross margin. Our global cost reduction program remains on track for expected run rate savings of $1.5 billion by the end of 2024 and $2 billion by the end of 2025.

Next, we experienced strong free cash flow generation behind profitability improvements, supporting further balance sheet strength. The progress on reducing our leverage has been significant in 2024.

And finally, we have deployed new investments to stimulate sustainable growth with the primary goal of reinvigorating share gain to achieve organic growth at 2 to 3 times the market over the long-term.

Through our transformation, we have stabilized the company and are setting a solid foundation for future growth and significant EBITDA expansion. We're also strengthening our organizational culture to be centered around organic growth with an operational excellence mindset, which we expect to carry forward into the future for the next decade.

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The entire Stanley Black & Decker team has persevered through challenges and with hard-earned self-generated momentum behind us, we have conviction that there are solid value creation opportunities in the short-, medium- and the long-term.

As we look at our markets in aggregate today, they remain relatively stable on the surface. That said some continue to be pressured by the continuation of mixed consumer trends, especially related to housing as well as weak automotive production backdrop. These factors are informing our current focus to refine and improve agility within our current cost structure.

At the same time, we are funding new growth investments in the relatively healthy pockets of our business such as DEWALT professional tools, which gained share for the sixth consecutive quarter. We are optimistic that the markets will turn in our favor in the future as interest rate cuts in many geographies likely will prove to be an initial catalyst. There will be a lag between lower rates and the flow-through to demand for our categories, and we expect choppy markets will extend into the front half of next year until interest rate reductions have a greater effect and the US election result is known and settled.

As a short-cycle business, we will plan our production and inventory thoughtfully to ensure we are ready for stronger demand in the future, which could be as early as the second half of 2025.

Before I get into the third quarter results, I'd like to mention our upcoming Capital Markets Day on November 20 at the New York Stock Exchange, which will also be available via live webcast. The leadership team and I are looking forward to hosting this event.

We will use it as a forum for key leaders, many new to the company with fresh perspective, to share more about how the operational changes implemented over the last two years set us up for future success. We will discuss what is next as we continue to position the company to deliver higher levels of organic revenue growth, profitability and cash flow over the long term, which will drive strong long-term shareholder return via significant EBITDA expansion. If you are interested in attending, reach out to Dennis and the IR team for more information.

Now shifting to the third quarter results. We delivered $3.8 billion of revenue, down 5% versus the prior year with organic revenue down 2 points. Volume was down 3 points on a weak consumer backdrop and mixed end market demand, which was partially offset by 1 point of price. We capitalized on pockets of relatively healthy market demand and delivered our sixth consecutive quarter of DEWALT growth as well as higher sales in aerospace fasteners.

The infrastructure divestiture, which closed early in the second quarter was a 2 point drag. Currency had a negative 1 point impact to revenue.

Adjusted gross margin was 30.5%, up 290 basis points versus the third quarter of last year, a step-up primarily attributed to the supply chain transformation. Adjusted EBITDA margin was 10.8%, which is up 140 basis points versus prior year. This was driven by our gross margin expansion partially offset by prioritized investments designed to deliver future market share gains.

Adjusted diluted earnings per share was $1.22 for the quarter. Free cash flow was approximately $200 million in the third quarter, which provided capacity to reduce debt by $100 million. Strong cash generation continues to support our ongoing capital allocation priorities, namely shareholder dividends, balance sheet strength and organic investments.

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Finally, we are narrowing our 2024 full year adjusted diluted EPS guidance range to $3.90, up to $4.30 and reiterating our free cash flow guidance of $650 million to $850 million. Pat will provide more color on this later in our presentation.

I want to thank our team members for their persistence in staying focused and forging ahead despite a choppy macro environment. We continue to make substantial progress on our transformation plan and achieve the financial milestones we established over two years ago. We will remain committed to our investments for share gain and the margin expansion journey that is generally within our control.

I will now pass it to Chris Nelson to review the business segment performance.

Christopher J. Nelson

Chief Operating Officer, Executive Vice President, President-Tools & Outdoor, Stanley Black & Decker, Inc.

Thank you, Don, and good morning, everyone.

Beginning with Tools & Outdoor, third quarter revenue was approximately $3.3 billion, down 2% organically versus prior year. DEWALT was a bright spot, delivering its sixth consecutive quarter of organic growth as the brand continues to attract demand across the Tools & Outdoor product line. Price was plus 1% in the quarter, a weak consumer and DIY backdrop contributed to volumes declining 3%, with currency impacting revenue by another 1%.

Third quarter adjusted segment margin rate was 11.1%, a 180 basis point improvement compared to the third quarter last year. Our supply chain transformation continues to help us deliver year-over-year margin expansion, while also funding our deliberate increase in growth investments.

Turning to the product line performance for the third quarter. Power Tools declined 1% organically due to softness in consumer and DIY brands. On the positive side, DEWALT cordless products grew in the quarter. Volume was also supported by the initial holiday season sell-in across our priority brands. We are excited by a great lineup of offerings that will be available to our end users in the fourth quarter.

Hand Tools faced similar pressure from the consumer environment and organic revenue was down 3%. However, we saw a strong customer response to our recent product launches of the DEWALT TOUGHSYSTEM 2.0 DXL storage lineup as well as our expansion in the material handling space with the construction jack. These innovative new products designed to enhance end user safety and productivity were meaningful contributors to the DEWALT sales growth in the quarter.

Outdoor organic revenue declined 3%, pressured by what we believe to be the final innings of destocking within the independent dealer channel.

Turning to performance by region. North America declined 4% organically, driven by the same factors as the overall segment. European revenue grew 1% organically despite a soft market backdrop. This was driven by double-digit growth in both Central Europe and Iberia, which more than offset pressure in the UK. We are prioritizing investments to advance our regional presence and accelerate new product listings. These investments are designed to support market share expansion and will serve us well as our customers become more optimistic on the prospects for market growth.

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Our remaining regions, outside North America and Europe, in aggregate, delivered solid performance, generating 6% organic growth. This was driven by double-digit growth in Latin America, led by Brazil, along with high single-digit growth in India.

In summary, for Tools & Outdoor, growth in DEWALT was once again the highlight, along with the strong segment margin performance.

As we look ahead, we remain focused on our efforts to continue to improve our gross margins and further strengthen our growth culture. Focusing on these two core imperatives allows us to prioritize resources and make new investments behind our best prospects for share gain.

Now moving to Industrial. Third quarter revenue declined 18% on a reported basis versus the prior year, which was nearly all attributable to the Infrastructure business divestiture. Organic revenue was down 1% as market softness in automotive contributed to segment volumes declining 2%, which was offset by 1 point of price.

Automotive was down double-digits, as OEMs reduced light vehicle production schedules and constrained CapEx spending. The aerospace business grew 22% organically, supported by new content wins and a strong booking rate. General industrial fasteners was up low single-digits, and we were pleased to see this business return to growth after prolonged customer destocking.

The Industrial adjusted segment margin rate was 13.9%, an improvement of 170 basis points versus prior year, driven predominantly by price realization and cost control. This performance is notable given the mixed market conditions. We are encouraged to see the enterprise-wide transformation efforts resulting in adjusted operating margin expansion across both segments.

Moving to the next slide. I would like to highlight a couple examples of how we are thoughtfully and aggressively prioritizing resources to accelerate growth in Tools & Outdoor.

First, we have committed to investing $30 million by 2027 in initiatives to support tradespeople and their priorities, including skills development. There is a shortage of tradespeople today, and they are both our core end users and in high demand. We've already invested more than $10 million in the program and related initiatives since its inception and will continue to fund this commitment. The program is designed to grow the number of skilled tradespeople, which means investing both in initiatives to support newer generations entering into the trades as well as to upskill tradespeople that are already established in their careers.

Helping to solve the gap in trade skills is important not only to support the communities we serve, but it is also key to unlocking future growth in our industry. These investments also advance our end-user focused business strategy. By investing more to promote the long-term vitality and success of our professional end users, we can support both newer generations and established tradespeople to help expand trades capacity building deeper connections with our end users while amplifying DEWALT's strong brand loyalty.

To highlight a couple recent examples where we partnered with organizations that share our commitment, on September 20, in honor of National Tradesperson Day, we announced that DEWALT awarded nearly $4 million in Grow the Trades grants to 166 organizations in the United States and Canada, focused on skilling, reskilling and upskilling tradespeople. DEWALT also sponsors trade scholarships to support education in fields, including the concrete, mechanical, finishing and pipe trades.

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We are also proud of our long-standing partnership with WorldSkills. This year, the competition in Lyon, France, DEWALT was the Platinum Partner. STANLEY and FACOM were also featured as official tools partners.

One final highlight I'll share is our recent participation at the Tradeswomen Build Nations Conference in New Orleans. At our booth and throughout the event, our DEWALT team members spent time getting to know the tradeswomen better, their personal experiences, challenges and aspirations. You're accustomed to hearing from us about new product innovations, but these investment programs are just as important. They are creating a virtuous flywheel by supporting our end users today to create more sustainable demand in the future.

And as I shared last quarter, our loyal end users are one of the top essential attributes for success. We continue to prioritize building deeper connections with these end users to deliver purpose-built innovation.

Another key attribute for success is our differentiated innovation engine. As a leader in total job site solutions, we are focused on continuing to empower tradespeople on the job site by optimizing user workflow, productivity and safety.

The recent unveil of the 20V MAX GRABO LIFTER is one of several new additions to DEWALT's ecosystem of tools and technology that provides end-to-end solutions designed for trade professionals. The GRABO utilizes a powerful electric vacuum pump to help maximize user control during lifting, carrying or installation applications for a wide range of heavy construction materials.

This is just one example of how we are focused on driving robust innovation to help solve the most pressing challenges our professional end users face, particularly to enhance safety and productivity on the job site.

Our talented team is moving with speed and a clear mandate, executing our transformation plan and accelerating share gain. We are focused and organized and we believe we are well positioned to deliver sustainable, profitable growth.

Thank you very much. And I'll now pass the call over to Pat Hallinan.

Patrick D. Hallinan

Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

Thanks, Chris, and good morning. As Don shared, we continue to make meaningful progress on our transformation journey. I will now highlight our financial accomplishments during the third quarter and detail our focus on delivering our 2024 objective and our margin progression in 2025 and beyond.

In the third quarter, we achieved approximately $105 million of pre-tax run rate cost savings, bringing our aggregate savings to approximately $1.4 billion since the program's inception.

Our third quarter and program to-date performance demonstrates strong execution by employees across our organization. We are tracking to plan, driven by consistent progress across our work streams. We are diligently capturing cost efficiencies amidst a backdrop of soft demand and freight inflation, as we complete the transformation and pursue the actions needed to meet our gross margin objectives.

Stepping back, we continue to target $1.5 billion of pre-tax run rate savings by the end of 2024 and $2 billion of pre-tax run rate savings by the end of 2025. We are on track to achieve both targets as we work towards our 35%-plus adjusted gross margin target.

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As a reminder, our core supply chain transformation savings initiatives are strategic sourcing, operations excellence, footprint actions and complexity reduction. Strategic sourcing remains the largest contributor to our transformation savings to-date, driven by component-related savings captured in 2024.

Sourcing activities are leveraging the advantages of a functional center of excellence; capturing economies of scale and rationalizing our supply base to focus spend on our critical strategic suppliers.

Operations excellence is the next area of opportunity, which translates to productivity improvements across our system. This initiative leverages lean principles, which are being implemented at targeted sites throughout the globe.

We are optimizing our distribution footprint as well as redesigning our manufacturing network to leverage scale and centers of excellence, as we maximize operational efficiency.

Approximately one-third of our facilities are undergoing significant change during 2024. We expect this work to continue into 2025 and potentially beyond. We are well underway with our platforming strategy, as we identify methods to standardize parts and components across product families. The aim is simplicity which we will achieve by reducing complexity, improving procurement scale, and ultimately decreasing the cycle time of our innovation process.

We are combining this with a fresh design-to-value approach to better serve our customers at a competitive cost advantage. This method takes a holistic approach to designing and bringing new products to market faster, while also doing so more efficiently, which can generate material productivity and cost savings well beyond 2025. As much as it's a method, it's a mindset that we are instilling across the company as we continue to look for productivity enhancements going forward.

I would like to commend the organization for diligently pursuing the goals of our transformation, this journey would not be possible without everyone's contribution. The progress we've shared today, including developing a sustainable cost structure and generating operational efficiency gives us confidence in our ability to achieve our gross margin objectives for 2024 and to achieve 35%-plus adjusted gross margin as we work to close out the transformation. With that said, we believe this is not the end goal, rather a way point on the journey.

Moving to the next slide. During the third quarter, we continued to make progress on two main areas of focus; generating free cash flow and expanding gross margins to support investment in long-term profitable growth and share gain.

We generated nearly $200 million of free cash flow in the third quarter. This brings year-to-date free cash flow broadly in line with where it was in the prior year. That said, and importantly, the composition of free cash flow reflects a healthier mix.

In the current fiscal year, free cash flow is weighted towards cash earnings and benefits from transformation cost efficiencies in addition to working capital reductions, the latter of which dominated 2023 free cash flow generation. This shift in makeup is a strong signal that our profitability and operating improvements are translating to sustainable free cash flow generation.

We are reiterating our full year free cash flow guidance range of $650 million to $850 million. We expect fourth quarter cash generation to be supported by positive earnings, working capital reductions from a seasonal drawdown of receivables, as well as a modest reduction in inventory.

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Our 2024 outlook for capital expenditures is $325 million to $375 million, which is approximately $75 million lower at the midpoint than our previous assumption. This benefit for 2024 is offset by an expectation that we will carry slightly higher levels of inventory at year-end versus our July guidance.

With that in mind, we are taking a measured approach to inventory management in the back half of 2024 and into 2025, as we navigate potential changes to the external environment and our markets, including the possibility for an acceleration of demand.

Looking forward, we are planning to allocate free cash flow in excess of the dividend to support debt reduction, which we expect will result in a total gross debt balance that is a little over $6 billion as of the end of 2024.

Beyond 2024, we are planning for further deleveraging with the goal to achieve our targeted leverage metrics of approximately 2.5 times net debt-to-EBITDA by year-end 2025. We plan to achieve this objective by utilizing excess free cash flow beyond the dividend and modest portfolio pruning actions.

Turning to profitability. Adjusted gross margin was 30.5% in the third quarter, a 290 basis point improvement versus prior year, primarily driven by savings from the supply chain transformation net of normal wage and benefit inflation. We are planning for further sequential improvement in the fourth quarter, supported by our supply chain transformation initiatives. Our current plan puts us on the path to achieve our goal of approximately 30% full year 2024 adjusted gross margin.

Now turning to 2024 guidance and the remaining key assumptions. In addition to reiterating free cash flow guidance, we are guiding GAAP earnings per share range to $1.15 to $1.75 and adjusted earnings per share range to $3.90 to $4.30 with both ranges narrowed, but unchanged at the midpoint as compared to our prior guidance. Our outlook factors in the continuation of a relatively soft macro environment in the fourth quarter, one that is marginally weaker than that anticipated at the end of the second quarter, driven by continued consumer softness and global automotive production declines that appear to have yet bottomed.

As we have done throughout the year, we are leveraging the cost savings primarily within our control, to offset these pressures and generate adjusted EBITDA growth versus the prior year. At the midpoint of our guidance, we are assuming full year organic revenue will be down 1 percentage point with fourth quarter organic revenue declining approximately 1.5%.

Our full year total revenue guidance, at the third quarter ending foreign currency rates, is relatively similar to our prior revenue guidance as recent currency rates are less negative than previously forecast offsetting the moderate incremental weakness in organic revenue.

Turning to the segments. Our outlook for Tools & Outdoor full year organic revenue is unchanged at down 1% at the midpoint, plus or minus 50 basis points, with relatively flat pricing for the full year. We have updated our expectation for the Industrial segment to be down 1% at the midpoint, plus or minus 50 basis points. This assumption now incorporates more pronounced global automotive production headwinds than our prior guidance and assumes that the fourth quarter organic revenue will be in a similar zone to that at the end of the third quarter.

Broadly, we remain positive about our industry's long-term growth prospects. Near-term, we expect markets to remain choppy and soft until interest rate reductions have greater effect, global automotive production fully corrects, and the US election result is known. We remain committed to our investments for share gain and the margin expansion journey that is generally within our control.

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Turning to SG&A. We are maintaining a disciplined approach to cost management given the near-term market softness, while prioritizing investments for long-term organic growth. Our planning assumption for innovation, brand, marketing activation and technology growth investments remains an incremental $100 million in 2024. We expect full year 2024 SG&A, as a percentage of sales, to be in the low 21% zone.

We expect total company adjusted EBITDA margin to approximate 10% for the full year, supported by savings from the transformation program. Our adjusted segment margin assumptions for Tools & Outdoor and Industrial are relatively consistent with our prior plan and expected to be up year-over-year. Our adjusted earnings per share range is $0.40 with variability in market demand being the largest contributor between the high and low-end.

We remain focused on our goals for adjusted gross margin and expect to manage SG&A thoughtfully in this environment, while working hard to make the investments that position the business for long-term growth.

Turning to other elements of guidance, GAAP earnings include pre-tax non-GAAP adjustments ranging from $455 million to $485 million, unchanged at the midpoint versus prior guidance.

These charges largely relate to the supply chain transformation program, the second quarter environmental reserve adjustment and the non-cash brand impairment charge from the third quarter.

The adjusted tax rate is expected to be 10% for the full year, which will imply a tax benefit in the fourth quarter. Other 2024 guidance assumptions at the midpoint are noted on the slide to assist with modeling.

In summary, we remain focused on executing our supply chain improvements to further improve gross margin and earnings. Our progress to-date supports our narrowed full year earnings and free cash flow outlook.

We remain confident that our actions to drive towards our target of 35%-plus adjusted gross margin, while funding additional organic revenue growth investments will continue to generate positive results.

Our top priorities remain delivering margin expansion, generating cash and further strengthening the balance sheet to position the company for long-term growth and value creation.

With that, I will now pass the call back to Don.

Donald Allan, Jr.

President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

Thank you, Pat. As you heard this morning, the company is making meaningful progress across our key priorities of margin improvement, cash generation and balance sheet strength, while also investing in future sustainable growth to drive share gains.

We are moving decisively to continue to deliver results despite mixed end market demand, which likely will continue through the middle of 2025. We will stay focused on this consistent execution while positioning the company to deliver higher levels of sustainable organic revenue growth, profitability and cash flow, which will drive strong long-term shareholder return via significant EBITDA expansion.

We are now ready for Q&A. Dennis?

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Dennis M. Lange
Vice President-Investor Relations, Stanley Black & Decker, Inc.

Great. Thanks, Don. Shannon, we can now start the Q&A, please. Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Julian Mitchell with Barclays. Your line is now open.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Hi. Good morning. Maybe...

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Morning.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

....just wanted – good morning. I wonder if you could flesh out a little bit how we're thinking about next year as a sort of within touching distance. So just wondered sort of – are you still confident about kind of 35%-plus gross margin exiting next year? And if we think about the sort of construct as it looks today, should we be thinking sort of first half of next year flat to down sales similar to how you're exiting 2024?

And then the margin expansion, it looks like operating margins, via exiting this year, up about 100 bps year-on-year in Q4. Is that a sort of a good placeholder early next year? And so next year, it's really about the second half when you see a big revenue and margin jump? Thank you.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Thanks, Julian. So yeah, we'll – I'll let Pat give some color and thoughts of where we are related to 2025. And then I'll circle back at the end with some perspectives on progress in the transformation and how we close out the transformation in the next 12 to 18 months. Pat?

Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Yeah, Julian, a lot in there. If I start with sales, I would say, we're not here to give precise 2025 guidance, but certainly, we expect the macros we're facing now to be characterizing the front part of next year. So, soft and choppy tools demand and probably still some auto headwinds into the front part of next year. So more likely than not we're expecting a flat to down start to the year. Obviously, we'll update that when we give guidance in the early days of 2025, but I'd say flat to down, more likely down is probably where we'd start.

And then on the gross margin, gross margin has been a key part of our journey and remains a key part of our journey. And certainly, we continue to work towards 35% in the fourth quarter of next year. But the transformation

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is about gross margin improvement. It's also about returning to share-driven growth and to getting the margin and the growth together to achieve $2-plus billion of EBITDA output from the business. And, as a team, we remain very confident in getting to 35%-plus and to getting to $2 billion plus EBITDA. The timing of that is going to depend on the headwinds.

We really feel like those are the right targets. But we've had a lot of headwinds in this journey. We are right now identifying and accelerating incremental activities to drive that margin expansion. And to the extent to which those accelerated activities are timed up enough relative to the headwinds. Again, we'll update you when we give guidance in the early part of next year. But that is certainly our focus, and it's going to be just a balancing act of the acceleration of our activities relative to the headwinds.

And then in terms of the margin in the early part of the year, I mean, I think we will be 31-ish in the fourth quarter of this year. And then it will be a little bit of a similar dynamic as we click into the first half of next year relative to the back half of this year, where you have some of the natural seasonal headwinds from the Outdoor business in the early part of the year plus some of the under absorption from the slow demand in the back part of this year. So, I do expect the year-over-year dynamics at least first half of 2025 to first half of 2024, to look a little bit in terms of incremental improvement, a bit like what you saw from 2024 to 2023.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

If I just kind of circle back to the overall broader transformation framework that we established about 2.5 years ago roughly. And we went into this journey knowing that there were a handful of things that we needed to address. And obviously, the first thing was developing a muscle around organic growth and gaining share that had not been consistently in place at Stanley Black & Decker over the last several decades. We grew through a lot of other things such as acquisitions that created a significant amount of value. And so, we continue to build that muscle, and that's an important part of this transformation. And both I and Chris made comments today and the progress in that journey, and we still have more progress to make.

The other thing was the profitability of the business and the cash flow and getting ourselves to 35-plus percent. We still feel very strongly in our ability to get above 35% gross margin. The timing of it, as Pat said, could vary a little bit but – due to headwinds and other factors. But as we've gotten deeper and deeper into this in the last 18 months, as we've worked together as a team, we see a lot of value drivers for the next three or four years that can continue to improve our margins and allow us to continue to invest more into the front end of the business so that we can develop the strength and the muscle, so we do gain share on a sustainable long-term basis in our industry, which is something that we think is the biggest value driver of all once we get our margins above that 35%.

So more to come on that at Investor Day. We're excited to walk through more details in about three weeks from now. But we're very pleased with the progress, and we still are very committed to the overall objectives we established through the transformation 2.5 years ago.

Operator: Thank you. Our next question comes from the line of Chris Snyder with Morgan Stanley. Your line is now open. Chris Snyder, your line is open. Please check your mute button.

Christopher Snyder
Analyst, Morgan Stanley & Co. LLC

Q

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Oh, sorry about that. Thank you. I wanted to follow-up on the gross margin commentary. So, it seems like 2024, maybe you will exit the year up 150 basis points. And to get to that 35% at year-end 2025, you kind of need to then have 2025 be up 350, year-on-year, basis points. So, I mean – I guess, was the prior commentary basically saying that that's not a year-end 2025 target anymore, it's kind of more in the distance? And I know that it's macro dependent. So maybe if there's anything you can kind of say on the macro that's needed to get to that 35% to exit next year? That would be helpful. Thank you.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Yeah, Chris. I don't know that it's not the objective anymore. That's not what we said. We're still working towards it. It's really a question of given the headwinds the back part of this year, I'd say the back part of this year, our sales have been about 1 point lower than we expected, and we still feel like auto hasn't fully corrected. That's a pretty profitable part of our Industrial portfolio. And then while it's a smaller part of our portfolio, we'll probably see some blip next year from the Boeing strike.

So, it's just a question of will we tee up enough incremental and accelerated activities to offset that and any other headwinds that come our way. And we just don't want to get ahead of ourselves. We'll kind of update everybody on that when we get to guidance at the end of next year. It's still the working goal of our team.

I'd say what's really going to affect it probably as much or more than anything is at what pace do interest rates start taking effect. And how quickly does auto correct because that's a very profitable part of that Industrial business. And then how much fixed cost reduction activity will be able to both implement and complete in time for it to roll off the balance sheet next year. I think those will be the factors that affect that timing precisely.

But like I said, that's still our working goal. And yes, along the way, the headwinds have certainly made the slope of next year a little bit steeper than we would have preferred. But we have every confidence we'd get to 35-plus percent. In fact, we see good opportunities of platforming to go beyond that. So, I think the timing is just a match-up of headwinds versus accelerated activities.

Operator: Thank you. Our next question comes from the line of Tim Wojs with Baird. Your line is now open.

Timothy Wojs
Analyst, Robert W. Baird & Co., Inc.

Q

Hey, guys, good morning. Thanks for the color. Just a follow-up to that last question and then my question. So, I guess first, Pat, could you just talk about what the accelerated activity is and kind of what cost buckets you're kind of attacking because you guys are already taking out a lot of costs. I'm just kind of curious where the incremental pieces are?

And then second, just Don, as you kind of changed the mindset internally from maybe something that's more acquisition and kind of integration focus to organic focused. What are the biggest changes that you need to make to the organization internally to kind of get that algorithm right?

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Why don't you start Pat? I'll answer that second.

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Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Yeah. I'll start, Tim. I mean as you mentioned, yeah, we have a lot of streams of work going. I think when we're talking about 2025, and 2025 specifically, I think you're going to see acceleration on three fronts, sourcing, footprint and platforming, but the key to unlocking next year is probably more the middle one, footprint. But again, that's something we're still working internally, but we'll be pulling all three of those levers greater than expected. But I'd say the key to unlocking next year is some footprint action.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

And thanks for the question, Tim, on the culture aspect of shifting from heavily weighted towards M&A to an intense focus on organic growth and market share gains. And it is something that we've been working very hard at for the last 2.5 years. But in particular, in the last 12 to 15 months, as Chris Nelson joined us, and he's made some changes to his team. And so I'm going actually ask Chris to give some color on the things that we're doing within T&O. And then as we work through that, we'll begin to translate some of that over to Industrial. So Chris, why don't you give us some more color on that?

Christopher J. Nelson
Chief Operating Officer, Executive Vice President, President-Tools & Outdoor, Stanley Black & Decker, Inc.

A

Absolutely. So, thanks a lot for the question, Tim. I mean, first of all, I'd say the most important thing that we have been changing and leaning into is really our focus and alignment around our core brands, understanding that, yes, we produce products, but what our customers and end users count on us for is to be able to provide them the solutions that they need with the brands that they respect and trust. And I think that as we've organized more around a brand-centric culture and how we can then provide those solutions, that has been a significant cultural change to the organization.

Secondarily, really as well as the laser focus that we have on the brand building also making sure that we have a very clear focus on what end users we are serving and making sure that we are driving innovation that they need for their – to make their lives easier. Particularly making sure that with the professional end user, we are driving more purpose-driven innovation to make sure that we can enhance the safety and productivity of our professional end users on their job site and making sure that all the innovation that's going into our pipeline really serves that end goal and serves the brands that we are focused on.

From a third thing is, really then making sure that we are focused on our speed to market that as we identify which brands we want to grow and as we identify the key pain points we want to address of those professional end users that we can get those products to market quickly and effectively in an integrated manner and make sure that we get those tools in the hands of our end users to drive growth.

And then finally is, really making sure that we think in terms of driving investment into the front-end of the business, meaning that, we want to have our Stanley Black & Decker representatives meeting with our end users and our customers to make sure that we're supporting them explaining our innovations and driving share gain in the field and then working integrated marketing programs so that they can understand sample test and then ultimately purchase and utilize our tools going forward.

I think that pivot to driving the preponderance of our investment towards the front-end is kind of the final piece of the puzzle.

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Operator: Thank you. Our next question comes from the line of Jeffrey Sprague with Vertical Research Partners. Your line is now open.

Jeffrey Todd Sprague
Analyst, Vertical Research Partners LLC

Q

Hey. Thank you. Good morning, everyone. I guess just one follow-up on some of the outlook questions and comments and then something unrelated to that.

But first, just on – again, sort of on the outlook and the trajectory, you had been previously kind of pointing to that $2 billion-plus of EBITDA in 2026. Pat mentioned it again, but didn't say anything about the timeframe. Just wonder if your confidence on that is sort of slipping given the slow start to 2025?

And then my other question is just kind of help us think about what's going on with share in North America, you pointed to DEWALT gains that look like they are continuing and compounding on each other.

Just also I was a little mathematically curious though that North America sales in Tools underperformed each of your three categories, right, North America, down 4%, but [ph] PT (00:45:27) only down 1%, hand Tools & Outdoor down 3%.

So is there something else going on there, maybe speak to share on CRAFTSMAN and STANLEY brand? Or any other perspective you just kind of add on that complexion of the North American sales?

Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Hey Jeff, it's Pat. I'll take the outlook question and then I'll let Chris comment on US market share. So I would still say, no, our – we'll be very much targeting $2-plus billion of EBITDA by 2026.

In fact, I think kind of on a rolling four-quarter basis, that's probably somewhere in the front half of 2026. So I don't think anything has changed there. As I mentioned in the gross margin comments, we're accelerating initiatives to offset the headwinds, but we're also going to manage our total income statement to drive the EBITDA.

I mean, we recognize the value of driving EBITDA growth as quickly as possible. And so I don't think there's anything that's changed in terms of a meaning timeframe – a meaningful timeframe on EBITDA expansion. Like I said, probably on a rolling basis sometime in the front part of 2026, we're at that $2 billion-ish threshold.

Christopher J. Nelson
Chief Operating Officer, Executive Vice President, President-Tools & Outdoor, Stanley Black & Decker, Inc.

A

All right. Hey Jeff, this is Chris. Nice hearing from you. Just to provide a little more color on the share in North America. What I'd say is that, first of all, we're confident that we are stable to slightly growing our share over the course of this year for sure.

And as you pointed out, we've certainly been experiencing nice success in that share gain with the DEWALT brand. I think underlying that would be a little bit of the dynamic we have been talking about where that the Pro is relatively stronger than the DIY-er due to the – some of the underlying consumer trends.

And as a result, we certainly have seen that play out and impact the CRAFTSMAN brand more than the DEWALT brand. So I think that as we see that not only the strength of that brand continuing to grow, but that as we see the

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consumer strengthen as well. As we talked about thinking about somewhere in the back half of next year, we should see some of that additional momentum kind of compound what we're seeing with DEWALT.

Operator: Thank you. Our next question comes from the line of Nicole DeBlase with Deutsche Bank. Your line is now open.

Nicole DeBlase
Analyst, Deutsche Bank Securities, Inc.

Q

Yeah. Thanks. Good morning, guys.

Christopher J. Nelson
Chief Operating Officer, Executive Vice President, President-Tools & Outdoor, Stanley Black & Decker, Inc.

A

Good morning.

Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Good morning.

Nicole DeBlase
Analyst, Deutsche Bank Securities, Inc.

Q

Can you guys talk a little bit about what you're seeing on the cost side. Totally appreciate the additional pressures with respect to top line, but steel costs are down. Obviously, your component costs and input costs are much broader than steel. But if you could talk a little bit about what you're seeing there and how that's impacting gross margins?

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Sure. Nicole, I would say we kind of expected all year materials to be slightly down, freight to be slightly up. And I'd say, thematically, that's largely been the play that's been running. Where I would say is ground freight in the US has been a bit higher and a bit more persistent than we would expect. And so you kind of put the two together, you have some net inflation from ground freight, which – and the ground freight seems to be moving these days a bit more from labor cost and actual vehicle capital cost as opposed to fuel.

And so neither have been at extremes, I'd say just slightly higher headwinds from freight offsetting, as you mentioned, some of the material tailwinds that we would see. And I'd say for next year, at this point, we're kind of expecting kind of neutral price cost and no extremes in inflation or deflation.

Operator: Thank you. Our next question comes from the line of Nigel Coe with Wolfe Research. Your line is now open.

Nigel Coe
Analyst, Wolfe Research LLC

Q

Thanks. Good morning, everyone. Obviously, a lot of talk about the gradient of the gross margin improvement here. So is the message – the $2 billion of exit rates for next year is still in place, but we've got some volume and mix factors at play here. I just want to make sure that's the case?

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And maybe just, Don, just talk about the election and some of the scenario plan you've got in place there, obviously, if Trump wins, tariffs are in play. Just maybe just address that. Thanks.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

You want to take that first part, Chris?

Christopher J. Nelson
Chief Operating Officer, Executive Vice President, President-Tools & Outdoor, Stanley Black & Decker, Inc.

A

I'll start with the first part, Nigel. Yeah, I'd say we're focused on all three returning to share gain driven gross margin and EBITDA. And yes, the precise timing of 35% may alter slightly, but we still feel like on an exit run rate basis or a rolling 12-month basis, we're hitting that $2 billion EBITDA threshold in the first part of 2026, and that's still our focus, and we'll manage the total income statement to get there.

Donald Allan, Jr.
President, Chief Executive Officer & Director, Stanley Black & Decker, Inc.

A

Yeah. And on the tariff front related to the election. If Trump wins the election, we are likely in a new tariff regime. It is a question of the magnitude at this point, exactly how that will be rolled out and will it be specific to industries or more broad-based? How many countries will be covered in it? And so there's a lot of still unknowns associated with it.

However, as we've mentioned in previous settings, we have been planning for this possibility since the spring and have gone through a variety of different scenarios to plan for. And obviously, coming out of the gate, there would be price increases associated with tariffs that we put into the market. And so we've worked through a lot of that.

We'll continue to work through as if the scenario plays out and the tariffs become more concrete, we will work through getting those into the market in a reasonable timeframe, knowing that there's usually some type of delay given the processes that our customers have around implementing price.

The second thing is we've built a fairly robust plan of how we would mitigate over the next two years these tariffs by moving production and aspects of the supply chain to different parts of the world.

And some of that would be potentially moving things from China to other parts of Asia, maybe to Mexico, we'll see but likely to other parts of Asia. And so unlikely that we're moving a lot back to the US, because it's just not cost effective to do. And there's questions about whether we even have the labor to actually do that in this country.

So we have a fairly robust plan. What we don't know is which scenario is going to play out and exactly how that would be. Is it going be just China? Is it going to be every country? Is it going to be 60% China? Or is it going to be 25% China for everything? Those are all things that are to be determined. But I feel like we have a playbook on the shelf ready to go, depending if this scenario plays out.

And then obviously, we've been working our government relations activities very significantly over the summer into the fall to educate a variety of different politicians as to this industry and the dynamics of supply chain and how we serve our customers and how this would actually play out over the next two years. So that's an important part of the process as well.

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Operator: Thank you. Our next question comes from the line of Adam Baumgarten with Zelman & Associates. Your line is now open.

Adam Baumgarten
Analyst, Zelman Partners LLC

Q

Hey guys. Just on the path of gross margins from here. [ph] Obviously, know (00:53:34) the implied 4Q, should we expect gross margin to step down sequentially in 1Q and then move higher quarter-over-quarter from there next year, kind of like you saw this year?

Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Yeah, Adam, I don't know that I'd get that precise in the sense that we'll get into the early parts of next year, things that drive gross margin variability across the early months of the year are just the mix of outdoor relative to everything else.

And in this case, as we head into 2025, it will be a little bit of how much of the auto correction in our Industrials businesses, is starting to slow down or whether it's still in midstream.

And so I would just say, I think it's going to – broadly, if you look at half-to-half, you'll just see somewhere in the 31-ish percent, maybe 31%, plus or minus a few bps throughout the first half.

Maybe we can accelerate a few things and get it above that. But I don't know that I'd start getting specific timing fourth quarter to first quarter because those types of things are going to get into very specific shipment flows.

Operator: Thank you. Our next question comes from the line of Rob Wertheimer with Melius Research. Your line is now open.

Rob Wertheimer
Analyst, Melius Research LLC

Q

Thanks. Good morning. I wonder if you could unpack just a little bit more of the North American Tools & Outdoor? Maybe some of that is your channel partners' wanting a different inventory strategy? Maybe some of that is just weakness at retail? Maybe some of that is an expectation of a weaker holiday season? Just maybe give a sense of order of magnitude how the different factors are contributing to the [ph] sales part (00:55:25)? Thank you.

Patrick D. Hallinan
Chief Financial Officer & Executive Vice President, Stanley Black & Decker, Inc.

A

Yeah. So I think there's a few things in there. One would be that first and foremost, our POS was modestly negative in the quarter. And that's what we expected, and we had talked about that probably being the case as we – one of the dynamics is, as we rolled off of what was an earlier start to the outdoor season, we kind of normalized in Q3. Secondarily, we do see there being much more momentum and strength on the professional than there would be on the DIY-er.

And if you look at some of the underlying kind of metrics that we look at in the marketplace to explain that, there's obviously consumer sentiment, but then there's also the activity levels for R&R activity. which are notably down this year. And I think that, that's probably having a pretty significant effect on what we're seeing in the DIY-er as well.

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Moving forward, as we talked about, we don't see any real catalyst in the first quarter or first half that will change those dynamics, but we are optimistic on taking a look at the longer-term trends in our industry. And as we start to see some of the improvements in some of those longer-term construction spending, construction earnings, R&R activity, residential home starts, we'll see more progress and growth in the marketplace.

Operator: Thank you. This concludes the question-and-answer session. I would now like to hand the call back over to Dennis Lange for closing remarks.

Dennis M. Lange

Vice President-Investor Relations, Stanley Black & Decker, Inc.

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

Operator: This concludes today's conference call. Thank you for your participation. You may now disconnect.

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