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Stanley Black & Decker, Inc. (SWK)

Q4 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Fourth Quarter and Full Year 2023 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 2023 fourth quarter and full year webcast. Here today, in addition to myself, is Don Allan, President and CEO; Chris Nelson, COO, EVP and President of 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 11:00 AM today.

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This morning, Don, Chris and Pat will review our 2023 fourth quarter and full year results and various other matters, followed by a Q&A session. Consistent with prior webcasts, we are going to be sticking with just one question per caller.

And as we normally do, we will be making some forward-looking statements during the call based on our current views. 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 in our most recent 1934 Act filing.

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. Stanley Black & Decker's performance in 2023 reflects our relentless focus on the execution of our strategic business transformation, which resulted in us building a strong foundation for improved profitability in 2024. Stanley Black & Decker today is a more streamlined business, built on the strength of our people and culture with an intensified focus on our core market leadership positions in Tools & Outdoor and industrial. Despite a challenging market backdrop that pressured volumes during the year, adjusted gross margin improved in each quarter and we generated over $850 million of free cash flow. These results demonstrate significant progress against two of our most important areas of focus during 2023.

Here are just a few additional examples of our accomplishments from the past year. We improved the health of our cost structure as a result of the momentum from our supply chain transformation. We achieved our 2023 target and delivered over $1 billion of savings program to-date. We remain on track for the expected $2 billion of savings targeted by the end of 2025. Our fourth quarter adjusted gross margin approached 30%. This result outperformed the plan as our team's accelerated efforts to deliver profit and cash in response to the soft volume environment.

Our strong free cash flow generation was primarily the result of $1.1 billion of inventory reduction, as we successfully executed our supply chain initiatives. We continue to actively manage our portfolio of businesses. In December, we announced the agreement to sell our Infrastructure business, and currently expect that transaction to close at the end of the first quarter. This aligns with our simplification efforts and focus on shareholder value creation while advancing our capital allocation priorities. We strengthened our leadership team with the addition of three new highly capable, seasoned and respected leaders in Chris Nelson, Pat Hallinan and John Lucas, each of whom brings a fresh and exciting set of perspectives.

Stepping back over the past year-and-a-half, we have transformed Stanley Black & Decker into a different company, refocused and reenergized. Together, our talented and motivated leadership team, along with our diverse and high-performing associates across the globe, are executing our transformation strategy with urgency and diligence to ensure we continue to achieve our goals. Our performance to-date is encouraging and reinforces our confidence in making investments to pursue the compelling long-term growth opportunities in the markets that we serve.

Shifting now to our fourth quarter performance, revenue was $3.7 billion, which was down mid-single digits versus the prior year, primarily due to lower outdoor and DIY volume, as well as Infrastructure customer destocking. Our profitability exceeded our plan, as we recorded adjusted gross margin of 29.8% in the quarter. Adjusted gross margin was up over 10 points versus the prior year and improved 220 basis points versus the third quarter. As a

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result of our focused efforts, this is the fourth consecutive quarter that we delivered sequential adjusted gross margin improvement.

We also reduced inventory by $240 million this quarter, which brings our total inventory reduction to $1.9 billion since mid-2022 when we began this journey. 2024 will be the next chapter of transformation, an opportunity to demonstrate our ability to further improve profitability and cash flow as we plant the seeds for future growth and success for Stanley Black & Decker. While it will be a transitional year, we are continuing to strengthen our foundation to create greater future earnings power. We will remain focused on delivering differentiated product innovation through our portfolio of world-class brands, implementing cost efficiency measures within our control, and driving share gain in our core markets, all aimed to improve margin, earnings and cash flow.

Turning to the markets we serve, our view is that these markets will remain dynamic in 2024. Overall, we expect relative strength in demand from professional tools and portions of our industrial markets. However, we believe the consumer and outdoor demand trends will continue to be weak. Together, this results in a modestly negative outlook in aggregate for all of our markets.

Our global trade-weighted GDP estimates are slightly positive, with US real GDP growth projected to slow but remain positive in 2024. Global commercial construction is expected to moderate and industrial tool markets are expected to remain supportive. The global industrial fastener end categories will be led by aerospace, while automotive and industrial production markets will be relatively flat.

There are a few key macroeconomic indicators that more directly impact our larger markets in North America, which are somewhat mixed. Examples of this mixed North American tools and outdoor market are as follows. New residential builds are forecasted to improve from current levels, yet remain modestly negative year-over-year, residential repair and remodel is currently expected to retract, and the outdoor power equipment industry continues to show signs of customer destocking, and we don't expect to pivot to growth during 2024.

In summary, we're focused on the Pro user and the healthiest market segments to generate share gains. We are prepared for weak consumer and outdoor demand trends to persist. The midpoint of our 2024 plan represents a continuation of the current demand environment, which, in aggregate, is slightly negative for all markets. We will remain agile and ready to serve incremental demand if it accelerates in the second half. We believe that with our powerful brands and strong innovation machine, we have the opportunity to capture new wins with our customers and outperform the market.

Our plan for the year is underpinned by the continued supply chain cost improvements that are broadly in our control. We expect to deliver gross margin accretion, earnings growth and strong free cash flow. Pat will discuss this in more detail in just a few moments. 2024 will be a year of focus, excitement and purpose, and it is fitting that we are celebrating the 100-year anniversary of DEWALT, a noteworthy milestone and a reminder that we have been revolutionizing job sites for a century. We will always relentlessly innovate for our pros and all our end users, allowing them to achieve better, safer and faster results.

I want to thank our 50,000-plus employees around the world for their persistence and commitment to our mission in 2023. They each have contributed to the progress we've made on our transformation journey.

Now, stepping into the business segment results. I will discuss our Industrial business performance and then pass it to Chris Nelson to review the Tools & Outdoor results. Fourth quarter Industrial revenue declined 4% versus last year. Price realization was more than offset by lower volume, which was driven by the continuation of customer destocking in Infrastructure. Within the segment, Engineered Fastening fourth quarter organic revenues were up

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7%. This includes aerospace growth of 27% and auto growth of 10%, as we benefit from recoveries in those markets. This growth was partially muted by market softness in general industrial fastening.

The fourth quarter Industrial adjusted segment margin was 11.1%, down 40 basis points versus prior year, as lower volume more than offset price realization and cost control. For the year, we are very pleased with the performance of our Industrial segment. While organic revenue growth was flat, Engineered Fastening, which is our focus moving forward within this segment, was up 6% organically, behind the strength in automotive and aerospace. The team delivered full year adjusted segment margin of 11.8%, up 210 basis points versus 2022. This expansion was driven by price realization and cost actions taken to improve productivity throughout the year. I want to thank the Industrial business team for their strong execution in 2023. And I'd like to especially thank the Infrastructure team for their valuable contribution to Stanley Black & Decker. I am confident that the business is positioned for a future of innovation and growth with Epiroc.

I will now turn the call over to Chris to review our Tools & Outdoor performance.

Christopher J. Nelson

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

Thank you, Don, and good morning, everyone. Now, turning to the Tools & Outdoor fourth quarter operating performance. Fourth quarter revenue was approximately $3.2 billion, down 8% organically versus prior year, as a result of lower volumes, primarily from soft consumer outdoor and DIY market demand, while price remained flat. We made substantial progress improving profitability through the year, driving adjusted segment margin to 10% in the fourth quarter. This was a sequential step-up of 70 basis points versus the third quarter and 900 basis points better than the fourth quarter of 2022. We achieved this by realizing lower inventory destocking cost, delivering supply chain transformation savings and capturing the benefits of shipping cost deflation, which were partially offset by lower volume.

Now, turning to the product lines. Organic revenue for hand tools declined 6%, while power tools was up 1 point organically, as Pro-driven momentum offset pressures in DIY demand. Outdoor was significantly challenged, as customers right-sized their inventory levels. We expect that trend to continue into the start of the 2024 selling season.

In Tools, we finished the year with a relatively stable market backdrop, supported by Pro demand. For example, power tools' organic performance improved each quarter in 2023 and exited in a growth position. This demonstrates the demand for our iconic Pro-centric DEWALT brand and the best-in-class products that we are bringing to the market. As the outdoor market achieves post-COVID normalization, we are focused on improving our cost structure while prioritizing investments to capture targeted share gain opportunities with customers and accelerating innovation in hand-held electrification, which is a growing and highly profitable category.

Now, turning to fourth quarter performance by region. North America was down 10% organically with the Tools product line down low-single digits. The commercial and industrial channel, which has a heavy professional user base, grew low-single digits organically. Fourth quarter US retail point-of-sale demand remained negative versus the prior year, but above 2019 levels, supported by price increases and strength in professional tools.

European organic revenue was down 1%, with outperformance in the Nordics and Italy, which generated double-digit organic growth, as we continue to invest in expanding our professional product offerings and activating new battery-powered innovations within the region. Emerging markets grew mid-single digits organically, excluding the impact from the Russia business exit. Including this impact, organic sales declined 1%. Solid emerging market performance was led by high-teens organic growth in Brazil, marking the seventh consecutive quarter of organic

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growth in the country. I want to thank the Tools & Outdoor team for their focused efforts throughout the year, which has positioned us well as we continue to focus on winning with our customers and capturing long-term profitable growth and market share.

Now, turning to the next slide, I would like to now introduce our new groundbreaking equipment system, DEWALT POWERSHIFT. We are proud to bring this to market later this year as it demonstrates the company's commitment to innovation and electrification for the pros. The DEWALT POWERSHIFT system was unveiled at the World of Concrete trade show last week and is designed to meet the critical needs of concrete professionals. The electrified line will allow the Pro to transition away from gas-powered equipment without compromising efficiency and performance.

Each of the six concrete tools in the system uses the DEWALT POWERSHIFT 554 watt hour battery and high-speed charger to streamline efficiency. The battery can deliver up to 5,000 watts of continuous power. That is equivalent to 6.5 horsepower and is designed to withstand the toughest job site conditions. The POWERSHIFT battery leverages pouch cell technology, which DEWALT first brought to the industry in October of 2021. Pouch technology enables the cordless job site of the future, bringing more power, runtime and efficiency.

Take, for example, the POWERSHIFT VIBRATOR used for concrete placement. It is 85% more efficient than gas vibrators in the market today. POWERSHIFT VIBRATORs deliver 60 continuous minutes of nonstop work, which gives the user about 30% more runtime than a tank of gas. There are electrified vibrators in the market today that can only deliver 15 minutes of runtime. Adding to the extended runtime, this tool is 5 pounds lighter than a gas unit, and is 10 pounds lighter than any other electrified unit available.

DEWALT POWERSHIFT represents the next addition to the 100-year legacy of the DEWALT innovation mission, to deliver comprehensive end-to-end workflow solutions. Raymond DeWalt's founding principles of innovation, safety and productivity remain the core ethos of our company today. DEWALT's future remains strong, and we will lead the way in empowering tradespeople to succeed while defining the next era of industry innovation and minimizing environmental impact.

Thank you. And with that, I'll 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. Turning to the next slide. I would like to highlight the progress we have achieved, streamlining the business and transforming our operations. We are on track to deliver our $2 billion pre-tax run rate cost savings target by the end of 2025. We achieved approximately $160 million pre-tax run rate cost savings in the fourth quarter, bringing our aggregate savings to over $1 billion since program inception. This performance is slightly ahead of plan, as our teams accelerated savings efforts to offset macroeconomic volume headwinds that were greater than expected throughout the year, including during the fourth quarter.

Strategic sourcing initiatives remain the largest contributor to our supply chain transformation to-date. In addition to the program, freight rate and demurrage savings also contributed to margin improvement, starting early in 2023 and holding throughout the year. Consistent with expectations set at transformation inception, we expect strategic sourcing to be the leading contributor to savings, and we expect this to be the case in 2024.

Our operations excellence program continues to leverage lean manufacturing principles to improve productivity across both business segments. This work stream will expand in scope during 2024 and drive further cost

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efficiency in our manufacturing base. The footprint-related projects are progressing on schedule and production transfers into centers of excellence are in the various stages of qualification, testing and execution.

Similarly, logistics network optimization programs are also on track with regional distribution center redesigns underway. Concerning complexity reduction, our teams have identified approximately 85,000 SKUs for discontinuation and are assisting customers as they transition to replacement products. We have successfully eliminated over 45,000 SKUs as of the end of 2023, with more expected in 2024. These actions are expected to generate approximately $0.5 billion of savings in 2024, supporting the funding of additional growth investments in our core business.

As we move into the next phase of our transformation, footprint and product changes, such as those from platforming, will become more important and result in a lumpier cost savings trajectory as you would expect. We remain confident that our transformation can support the sustainable cost efficiency needed to return our adjusted gross margin to 35% or greater.

Moving to the next slide, two of our primary areas of focus during 2023 were free cash flow generation and gross margin expansion. We reduced inventory by approximately $240 million in the fourth quarter, inclusive of approximately $100 million attributable to the Infrastructure business held for sale accounting. This brings our inventory reduction to approximately $1.1 billion in 2023 and $1.9 billion since the middle of 2022. Our disciplined inventory reduction efforts throughout the year supported $853 million of free cash flow generation, which we used to fund our dividend and reduce debt by approximately $280 million versus the prior year. We remain focused on working capital optimization in addition to improving profitability to generate significant free cash flow. In 2024, we plan to reduce inventory by $400 million to $500 million, as we continue to prioritize working capital efficiency.

CapEx is expected to range between $400 million to $500 million, increasing versus 2023, predominantly in support of the footprint-related transformation initiatives planned for 2024. These items, in combination with organic cash generation, underpin our full year free cash flow range of $600 million to $800 million. As a reminder, we expect a typical profile for our working capital as we build inventory for the 2024 Tools & Outdoor spring selling season, resulting in the typical first quarter operating cash outflow. Our priority for capital deployment remains consistent, making transformation investments, funding our long-standing commitment to return value to shareholders through cash dividends and further strengthening our balance sheet.

Turning to profitability, adjusted gross margin of 29.8% in the fourth quarter was up 10.3 points versus the prior year, driven by lower inventory destocking costs, supply chain transformation benefits and lower shipping costs, which more than offset the impact from lower volume. Adjusted gross margin finished ahead of plan, as we intentionally accelerated supply chain transformation actions in 2023 while navigating weak consumer and outdoor demand and channel inventory conservatism to meet our profitability and cash flow objectives.

Additionally, pricing was 0.5 point better than our expectation, due to lower promotional mix in the quarter. We will continue our measured and disciplined approach to cost management to moderately improve on our second half 2023 adjusted gross margin gains into the first half of 2024, while managing the margin pressures that accompany the outdoor selling season. This is notable, given that we were able to deliver second half 2023 adjusted gross margin 1 point above the high end of our initial 2023 guidance, demonstrating the transformation is on our targeted trajectory.

We are planning for adjusted gross margin to approximate 30% for the full year 2024, and expect to exit the year in the low-30s, consistent with prior expectations. We are leveraging our $0.5 billion of cost reductions from the

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supply chain transformation and working hard to navigate another year without a macroeconomic tailwind. We made significant progress throughout 2023 on our journey to restore our historical 35%-plus adjusted gross margin, and our efforts are enabling incremental investments to accelerate long-term organic revenue growth.

Now, let's turn to our 2024 guidance and the remaining key assumptions. To reiterate, we are planning for 2024 to be another year where we prioritize cash flow generation and gross margin improvement. We are initiating a full year free cash flow guidance range of $600 million to $800 million, GAAP earnings per share range of $1.60 to $2.85 and an adjusted earnings per share range of $3.50 to $4.50. We expect relative strength in demand for professional tools and some of our industrial markets. Conversely, we are prepared for weak consumer and outdoor demand trends to persist. Together, these dynamics result in a modestly negative outlook in aggregate for our markets.

We are planning for organic revenue to be relatively flat at the midpoint, supported by targeted share gains in our businesses. Our EPS range contemplates plus or minus 2 points of volume growth with the variation representing the market demand scenarios in the plan. Tools & Outdoor organic revenue is expected to be relatively flat at the midpoint, behind our focus to win with the Pro through industry-leading innovation, investments in field resources and consumer share gains, leveraging our strong portfolio of brands.

The Industrial segment revenue is expected to be relatively flat to slightly positive organically, primarily driven by aerospace market recovery, as well as leveraging our core business model and electrification to deliver share gains. Industrial growth in 2024 is expected to be moderated by Infrastructure destocking in Q1 before the closure of the signed divestiture and expected softness in general industrial fastening markets.

We will continue to invest for long-term organic growth and share gain throughout 2024 and plan to invest an incremental $100 million to accelerate innovation, market activation and to support our powerful DEWALT, CRAFTSMAN and STANLEY brands. Our planning expectation is that SG&A as a percentage of sales in 2024 remains consistent with our recent fourth quarter, around 21%, which includes investments.

Turning to profitability, we expect total company adjusted EBITDA margin to improve to approximately 10% for the full year, supported by the benefits of the transformation program. Segment margin in Tools & Outdoor is planned to be up year-over-year, also driven by continued momentum from our ongoing strategic transformation. The Industrial segment margin is expected to be flat to up slightly versus prior year, as operating improvement in Engineered Fastening is offset by the dilution from the previously announced divestiture of the Infrastructure business.

For additional context around Infrastructure, our guidance assumes approximately $100 million of first quarter sales with the divestiture closing at the end of the quarter. Thereafter, we have excluded a profit and assume the proceeds will be used to reduce our commercial paper debt balance. With these assumptions, we've established a $1 adjusted EPS range, with the largest contributor being market demand variability. We will work to optimize adjusted gross margin through our transformation program, we will manage SG&A thoughtfully throughout the year given the macro uncertainty, but we will be working hard to preserve investments to position the business for longer-term growth.

Turning to the other elements of guidance, GAAP earnings include pre-tax non-GAAP adjustments ranging from $290 million to $340 million, largely related to the supply chain transformation program with approximately 25% of these expenses being non-cash footprint rationalization costs. Our adjusted tax rate is expected to step up in 2024 to 10%, with the first three quarters generally in the mid-20s. Discrete tax planning items are expected to reduce the full year rate and we currently expect these to occur in the fourth quarter.

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Other 2024 guidance assumptions at the midpoint are noted on the slide to assist with modeling. We expect the first quarter adjusted earnings per share to be approximately 13% of the full year at the midpoint. The EPS for the first quarter is impacted by the tax profile I discussed earlier, and a heavier contribution from interest expense associated with the expected first quarter commercial paper debt balance.

Adjusted first quarter EBITDA as a percentage of the full year is expected to be over 20%, consistent with pre-pandemic history. First quarter total company organic sales growth is expected to be down low-single digits, primarily due to the same factors driving fourth quarter 2023 softness. Adjusted EBITDA margins are planned to be up strongly versus prior year, leveraging the carryover benefits of the program and comping the destocking period.

In summary, 2024 represents another step along our transformation journey, with a continued focus on gross margin and cash while targeting share gains in a stable but tough macro environment. We believe our actions continue to position the company for long-term growth and shareholder return.

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

Donald Allan, Jr.

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

Thank you, Pat. We embarked on a bold transformation in the middle of 2022 to set Stanley Black & Decker on a path to drive strong long-term shareholder returns through sustainable growth, profitability and cash flow improvements. As we report another quarter of progress, our consistent execution against our plan gives us the confidence to increase investments, supporting the acceleration of organic growth behind our most powerful brands, particularly DEWALT, CRAFTSMAN and STANLEY.

In the face of dynamic markets, we're focused on delivering best-in-class product innovation, implementing cost efficiency measures within our control and driving share gain in our core markets. I am confident that we are creating a stronger and more focused company, capable of gaining market share consistently over the long term with the best people, the most iconic brands and the highest quality innovation engine in the industry.

With that, we are now ready for Q&A, Dennis.

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.

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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.

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

A

Good morning.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Good morning. Maybe just a question for me around that rate of improvement as we're going through the year. Just trying to understand, I guess, particularly the gross margin delta and also on the free cash flow progression. What's the confidence that, that gross margin can sort of move up sequentially as you go through the year to get to that low-30s exit rate? And on free cash, kind of how weighted should that $700 million midpoint be to the second half? Thank you.

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

A

Hey, Julian, it's Pat. Thanks for the questions. Our focus next year is on both of these topics, gross margin and cash delivery. And as we moved through 2023 and made very strong progress on gross margin, we certainly had the benefit in 2023 of that progression being the – the consumption of high-cost inventory out the balance sheet. So, throughout 2023, you saw a very, very significant degree of progression throughout the year. Throughout 2024, we're confident in our plan, and we're targeting the 300 basis points roughly of progression throughout the year. It will be back-half weighted. And then part of that is the low volume that we saw the back half of 2023 and expect to see the front half of 2024, but we have every confidence we're going to deliver it.

And as we started talking to investors at the back half of last year, we guided people to measure our gross margin progress in half-year increments. And if you look at the back half of 2023, we were about 28.7% for our back half of 2023 progression, and we expect to be in – in expansion mode, the front half of 2024, it will be modest in the 50-ish basis point range. And we'll be stepping up more significantly in the back half of 2024 as we accelerate some of the savings efforts we have on the docket for the year quickly to offset some of the volume softness we've been experiencing in the last 6 to 12 months. But we have every confidence we're going to get there.

In terms of cash, the main difference in cash year-over-year is really the difference in the transformation initiatives that are planned for 2024, where we're doing a bigger proportion of the footprint moves, which are going to drive more CapEx during 2024 than during 2023, about $100 million, and more cash-oriented restructuring charges around $50 million. So, the big difference year-over-year in cash drivers are the restructuring agenda. If you look at the rest of the cash drivers, we're still targeting pretty meaningful inventory reduction, but less than the $1 billion that we drove off the balance sheet in 2023. We're going to be in the $400 million to $500 million range. But that difference in inventory reduction is made up by a higher operating profit. So, those two things roughly offset

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each other, and the drivers are really the difference in year-over-year CapEx and the difference in year-over-year cash restructuring charges.

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

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

Q

Yeah, hey, guys. Good morning. Nice job on the margins. Maybe just – I had two cost questions. So, first, just on investments, Pat, what are you kind of explicitly investing or at least what's planned to be invested in 2024? And how variable are you kind of planning to manage those investments as you go through the year?

And then secondly, just on cost inflation, could you give us just an idea of kind of what you're seeing in kind of key cost inputs? And then also, what's kind of explicitly baked in for price/cost?

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

A

Yeah. So, on investments, we're continuing to invest predominantly in innovation and then in the field and marketing resources to activate it. So, of the $100 million we're targeting for 2024, I'd say three-quarters or more are around that. Obviously, a lot of that in our biggest business, our Tools & Outdoor business, but some in Industrial as well. It's mostly about innovation and market activation and field resources to support it. Maybe 20% to 25% is another capability building, to make us a more productive organization.

And then, as we go through the year – I mean, obviously, we're going into a year with a pretty muted macro and the uncertainty we've been experiencing in the last 12 or 18 months, we're certainly going to be paying close attention to the macro and managing our cost structure as we go throughout the year to be in step with that macro. But we are really focused on the long-term growth of this business. And we're going to be working hard as a leadership team and as an organization to preserve those investments even if the macro creates a bit more headwinds than we're expecting because we're not going to just completely collapse 2024 investment at the risk of longer-term brand health and brand share gaining power.

In terms of inflation and deflation for the year, our plan expects roughly flat across kind of materials and freight. You've obviously had some of the battery metals go down in significant percentage terms. But in dollar terms, those don't drive our basket as much as some others. There's been some recent upticks in steel, resins, and we'll probably face some marginal pressure from Red Sea freight. But overall, you put metals and freight together, roughly flat, still kind of a high labor rate environment, but that's embedded in our gross margin and SG&A assumptions.

And then finally, price/cost, again, roughly neutral. We'll have some carry-in price in Industrial, that's to the good, offset by just the normalization of promotional cadence in Tools & Outdoor. Again, recall, the back half of 2023, we're getting back to a normal promotional cadence as our supply chain healed, and that will be playing through the front half of 2024 as well. But I'd say, those two forces together, enterprise-wide, get us to roughly flat price dynamics for the year. And again, a roughly flat inflation backdrop in total.

Operator: Thank you. Our next question comes from the line of Chris Snyder with UBS. Your line is now open.

Chris Snyder
Analyst, UBS Securities LLC

Q

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Thank you. I just wanted to follow up about the flat lining of gross margin that's expected into the first half relative to the Q4 exit rate. It seems like there is a lot of savings on the balance sheet that is yet to flow through the P&L. And I think the expectation is that those come through on a couple of quarter lag. So, just maybe why is that not coming through in the first half? And I understand the Outdoor mix will pick up, but I would also think that Tools gross margin gets better from Q4 into the first half as you move past the holiday promo. So, any color on the gross margin delta between those product lines to help understand that mix would be helpful. Thank you.

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

Yeah, yeah. No, like I said, we do expect some modest expansion front half to front half. We had, as we went through 2023 and we saw volumes being really soft, I think, commend the team for still delivering over $500 million of savings across the volume backdrop that was for the year about 300 basis points or 400 basis points below what we expected, and we got beyond the high side of our guidance for 2023 gross margins. So, we came out at quite a strong rate.

As you point out, the trajectory in the first half is positive even if a bit muted. And I'd say, the couple of forces of that are one that you pointed to, you have a heavier Outdoor mix in the first half of the year, and you have some of the under-absorption that you – that was associated with low volumes from the back half of 2023. And those are really the two forces and they play out in the front half by muting some of the rate of that progress, but they don't take us off track for the full year savings.

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

Thank you. Good morning, everybody.

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

Good morning.

Rob Wertheimer
Analyst, Melius Research LLC
Q

My question is on dynamics – yeah, thank you – at the retail channel. And if I understood it right, you had volumes a little soft, you had promotional activity down, which is good. And I'm just curious about how that works out in market share, whether the competition is stepping up promotional activity, whether channel inventory [ph] has now (00:40:11) normalized, there is less promotion. Maybe just give us a comment on market share, on promotions, on dynamics of retail? Thank you.

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

Sure. Thanks, Rob. And – yeah, I think the competitive landscape has not really shifted or changed, as we went through the end of 2023 into the early stages of 2024. There's modest movements in certain brands moving across retailers. But aside from that, we're not seeing unusual pricing or discounting happening. And for the most

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part, it's really all of us navigating a somewhat muted market right now and continuing to position ourselves for share gain. But I'll ask Chris Nelson to give a little more color on what he is seeing.

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

Yeah. I'd say that if you think about the – just referencing POS, I would say that the POS played out roughly as we would have planned it in Q4, where we saw it was down year-over-year, but above 2019 levels. And if you think about the kind of buckets they're in, we saw strength out of the Pro [ph] and we (00:41:18) expected level of kind of difficulties that we're going to see in the consumer and DIY segment. So, that's on plan. And it's what we're contemplating, as we said, moving into this year for that being a fairly stable macro that we're playing the backdrop against.

As Don referenced, we're not seeing major changes in the competitive dynamics. What we are seeing and we're excited about is getting back to our normal promotional rhythms as we have been able to take care of our customers and fill our – our fill rates [ph] have been improving, (00:41:53) and that's made a big difference in our opportunity to compete well in retail.

And then I think the final part of your question that you referenced was regarding inventory levels. And certainly, on a global basis, as people take a look at what is somewhat of a dynamic or a tepid macro, people are thinking about rightsizing their inventories for that environment. And we see that in -somewhat anecdotally in places like Europe in some of our professional channels. But when you take a look at the biggest chunks of the inventory where we have really clean data in our major retailers, we're at historical levels. We feel good where we are there positioned, and we think that, that's going to be kind of a neutral dynamic heading into 2024.

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, guys. Believe it or not, I was actually at World Concrete. I saw the new products, pretty impressive I'd say. So, congrats on that launch.

Just on – on the pricing, came in obviously better than last quarter in Tools & Outdoor. So, just wondering if – you talked about normalization of the promotional activity, and I'm just wondering maybe you pulled back in the fourth quarter and [ph] perhaps that kind of put (00:43:18) some of the – maybe the weakness in Tools & Outdoor. But just I'd really be curious on the footprint changes that you're making with the CapEx. Obviously, we got Trump talking about China tariffs. I'm just wondering if there's going to be a material change in your sourcing and footprint during 2024.

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

Yeah. So, Nigel, we'll have Chris answer your first question, and then I'll take the second question after he's done.

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

So, from a pricing perspective, Nigel – good to hear from you. I'm glad you were able to see the new products. Sorry, I missed you there. But no, we did not see a significant pullback in the promotional volume. What we saw

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was in overall – as we saw – as we said, more challenge in the overall macro environment that I think contributed to that more than anything. And as we transition into next year, we're expecting that pricing dynamic to stay fairly stable, and we're – we feel good about our plans there.

And overall, I think it's fair to say that, as Pat pointed out, we're at a – we're kind of at a neutral price/cost. We're not banking on a bunch of inflation. And as we take a look at in the rearview mirror, we have recouped a significant, but not all of the cost that we took on as we saw inflation. And so, keeping that neutral price/cost is important for our gross margin trajectory moving forward as well.

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

Yeah. On the comment on the footprint, I mean, yeah, the geopolitical dynamics continue to be intriguing and interesting for sure what may play out in the future. But as it comes to our footprint transformation, we started with an overarching strategy of finding ways to get closer to our customer with our supply base and our manufacturing [Technical Difficulty] (00:45:11) certain types of products that are high volume in particular. Other products, you have to focus more on the low-cost location. And so, you end up with a mixed geography of where you're manufacturing and how you're serving your customers. That hasn't really changed. What we continue to do is – part of the transformation, though, is develop centers of excellence for power tools, certain types of hand tools, certain types of outdoor products that leverage the expertise we have in these geographies, in Asia, in Mexico and in the United States and Eastern Europe.

We will continue to build upon that, which gives – eventually will give us the ability to flex supply from different geographies if the geopolitical landscape changes radically. That will take time to do. That's not something that will necessarily occur in the next 6 to 12 months. But as we continue on this journey and finish this transformation in the next two to three years, that's an outcome that we're looking to achieve. And so, we believe that's the appropriate way to address what's happening in the dynamic geopolitical space and we'll continue to evaluate that going forward as things shift in countries like the United States if they shift and make pivots as necessary.

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 & Associates
Q

Hey, guys. Good morning. Just on SKU rationalization, do you think that had any impact on the volumes in the fourth quarter or even the second half of 2023?

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

Go ahead, Pat.

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

Yeah. Adam, no – I mean, that program has been very thoughtful in weeding out complexity that's not creating value for end users or for our shareholders. And there's no major disruption by that by any stretch of the [ph] imagination (00:47:16).

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Operator: Thank you. Our next question comes from the line of Michael Rehaut with JPMorgan. Your line is now open.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

Thanks. Good morning, everyone.

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

A

Good morning.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

I had a question on the growth investments and just how to think about the cadence of that longer term. I think you talked about it a little bit earlier in the call, but [ph] can you (00:47:46) talk about in totality, I think, alongside the 35%-plus gross margin and enabling $300 million to $500 million of growth investments, I was hoping just to get a sense of what those investments were in 2023, what you expect them to be in 2024 and 2025. And how much of that is going to be kind of an ongoing level of investment and if that would all be on the income statement in the tools and storage or if there would be some in corporate? Thanks.

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

A

Yeah, Mike, I'll give you a few points. I'd say 2023 was a bit over $100 million, will be around $100 million for 2024. And as I referenced on an earlier question, it's about three-quarters around innovation and then the marketing and field resources to activate that effectively. And the rest of it is around capability building, some of it in our business segments, a relatively small amount of it in corporate.

And I think if you're getting to the broader question of you're sitting there with a model and you're trying to figure out is SG&A permanently at 21% of sales or something else, if that's kind of behind the essence of your question, I'd say as we get back to share gains, and as we jolt our brands and our innovation up for a few years, I expect in the medium term to be more in the back to the 20-ish percent range, if that's kind of what you're trying to unpack. But I would expect us to be elevated in 2024 and potentially in 2025 and in 2026 depending on the macro and some of the things we're prioritizing in the medium term around that 20-ish percent level. And then, I think beyond the medium term, to the extent we can be exceptional at driving gross margin improvement, the SG&A will move with the rate at which we can drive gross margin improvement.

Operator: Thank you. Our next question comes from the line of Eric Bosshard with Cleveland Research. Your line is now open.

Eric Bosshard
Analyst, Cleveland Research Co. LLC

Q

Good morning. You talked about normalizing promotions and you talked about I think volumes relative to 2019. Just curious if you could give us a little bit of insight into promotional activity relative to 2019, where we are now and what is embedded in the guidance and what you're seeing in the market in regards to an appetite for promotions either from consumers, professionals or retailers.

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Donald Allan, Jr.

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

A

Yeah. Good morning, Eric. So, I would say that the level of promotional activities we're at now and we would expect in 2024 is probably pretty consistent with what we experienced in 2019. And so, we're kind of back to where we were, which I think was a healthy balance of normal core operating, selling activities and promotional activities. As we think about the year, our customers are not really talking to us about, what I would call, unusual levels of promotional activities. They're looking for the normal set of activities. And I think that's going to likely be the case throughout the year. And we tend to – in demand markets like this that are somewhat stable in the sense where you don't have a lot of growth and you don't have a lot of retraction, it tends to be a more normal promotional environment in that setting.

If demand retracts in a more significant way, then promotional activity does pull back a fair amount because the impact of promotions is not as significant. If we see a back half of the year that gets better, which there's – we talked about in that – in our presentation that our guidance doesn't necessarily include that, but if the back half demand environment is an improved environment, then you could potentially see a little bit of tick up in promotional activity related to that. But at this stage, based on our guidance, I think it's probably balanced to say that our view is that promotional activity will be consistent with what we saw pre-pandemic.

Operator: Thank you. This concludes the question-and-answer session. I would now like to hand the conference 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. Thanks.

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

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