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Stanley Black & Decker, Inc.

On November 2, 2009, the boards of directors of The Stanley Works, Inc. and Black & Decker Corp. agreed to a merger in which The Stanley Works would combine with Black & Decker through an exchange of stock giving Black & Decker's shareholders a 21.6% premium. Stanley would pay $3.6 billion in its stock (valued at Stanley's pre-announcement price of $45.23/share) for all of Black & Decker's stock. The merger would leave Stanley shareholders with 50.5% of the stock in the combined enterprise. Black & Decker shareholders would receive 49.5% of the stock of the combined enterprise. John F. Lundgren, age 57, the CEO of Stanley since 2004 would become CEO of the combined company while Nolan Archibald, age 66, and CEO of Black & Decker since 1986 would become executive chairman of the combined company.

Background

The Stanley Works was a hand tool company founded in 1843 and headquartered in New Britain, Connecticut. Black & Decker was a power tool company established in 1910 and headquartered in Towson, Maryland. Since the companies operated in similar lines of business, they had periodically discussed a strategic combination. Merger discussions had occurred in the early 1980s, the late 1980s and again in the early 1990s. These talks "typically stalled over who would be in charge."[1]

The Transaction Economics

Cost savings associated with the combination were a strong motivating factor in the proposed merger. The combined company was expected to save $350 million annually. The transaction was "… expected to result in nearly 4,000 layoffs from a global workforce of 38,000."[2] This level of savings would be achieved over three years at a cumulative one-time restructuring cost of $400 million (**Exhibit 1**). Stanley's GAAP earnings per share (once the full savings were realized at the end of year three) were expected to reach $5.00, an increase of $1.00 per share versus the EPS projection of Stanley without the merger (**Exhibit 2**).

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[1] Joann S. Lubin, "Black & Decker CEO Stands to Get Big Payday," *The Wall Street Journal*, March 10, 2010, p. B1.

[2] Lorraine Mirabella and Gus Sentementes, "A Md. Company Fades into Future: Black & Decker, With a 100-Year Past, Begins 'Day 1' on Monday Folded into Stanley Black & Decker," *Baltimore Sun*, 14 March 2010.

Professor William E. Fruhan prepared this case. This case was developed from published sources. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

The CEO and Other Officer Incentives

Shareholders would not be the only winners in the transaction. As part of the merger contract John Lundgren would receive "a grant of restricted stock units, the aggregate value of which will equal the value, as of the completion of the merger, of an option to purchase 1.1 million shares of Stanley common stock."[3] This would be in addition to his normal compensation contract. Nolan Archibald would receive a new three-year contract. While his annual compensation would be reduced somewhat as shown below, he would receive a one-time grant of stock options on 1.0 million of the combined company's shares plus a special incentive payment based on the amount of annual cost savings achieved by the third anniversary following the merger. The incentive payment would be $15 million if annual savings of $225 million were achieved, $30 million if annual savings of $300 million were achieved, or a total of $45 million if the projected annual saving of $350 million or more were achieved. He also agreed to forego a $20.5 million severance payment (golden parachute) in connection with the change in control.

Nolan Archibald Compensation

	Current Contract	Post-Merger Contract
	$ millions	
Base Annual Salary	$1.5	$1.5
Target Annual Bonus	$1.875 + $1.05[a]	$1.875
Maximum Annual Bonus	$3.750 + $1.575[a]	
Annual Equity Award	$8.5	$6.65
Special One-Time Awards	NA	Options on 1.0 million shares
	NA	$15.0-$45.0 for cost savings

Source: The Stanley Works, US SEC Filing Amendment No. 2 to Form S-4, February 2, 2010, pp. 76-78.

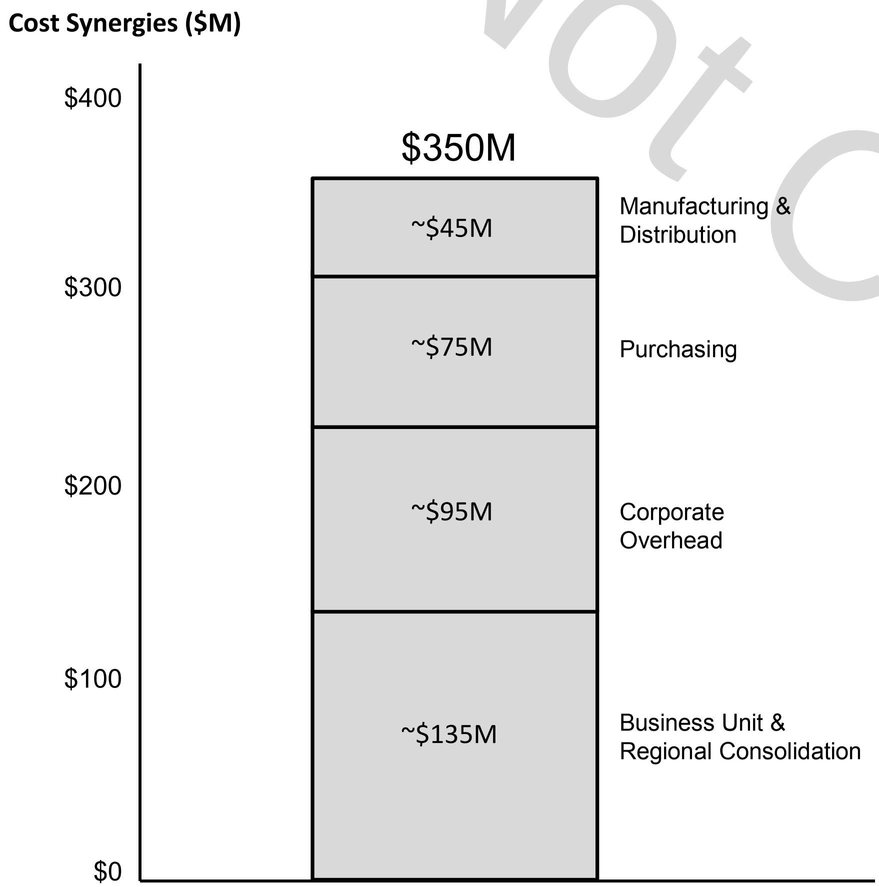
[a] Long-term incentive award

Nineteen Black & Decker executives (not counting Nolan Archibald) had change of control agreements extending back to 1986 which would trigger payments if they were terminated or experienced a change in responsibilities or powers as a result of the merger. Payments which could be triggered under these agreements for severance (3 years pay), benefits (3 years) and income tax gross-ups totaled $92.3 million. Payments under the B&D long term incentive plan (that would be triggered without regard to actual performance as a result of the merger) would amount to $13.2 million for these same 19 executives, and immediate vesting of all unvested restricted stock, restricted stock units and stock options would add $41.7 million to this total. Finally, additions to the B&D supplemental executive retirement plan for the benefit of five of these senior employees would total $22.7 million.

[3] The Stanley Works, "A Powerful Legacy, a Future of Growth," US SEC, Form 8-K Filing, November 3, 2009, p. 17, 19.

Exhibit 1 Amounts and Sources of Cost Synergies in the Proposed Stanley Black & Decker Merger

$350 Million Of Cost Synergies Identified (4% Of Pro Forma Sales)



Manufacturing and Distribution

- Plant Footprint Consolidation
- Distribution Network Consolidation

Purchasing

- Direct And Indirect Materials
- Freight

Corporate Overhead

- Public Company Costs
- Management, Facility And IT Integration

Business Unit & Regional Integration

- Management And Sales Force Integration
- Regional Shared Service Consolidation

One Time Cost To Achieve

- $400M Over Three Years

One Time Cost Of $400 Million To Achieve

Source: The Stanley Works, "A Powerful Legacy, a Future of Growth," US SEC Form 8-K Filing, November 3, 2009, p. 17.

Exhibit 2 Timing of Cost Synergy Benefits and EPS Impact from Proposed Merger

Pro Forma Financial Impact To Stanley

Creates A Global Leader With Pro Forma 2009E Revenues Of $8.4B

EBITDA Of $1.3B Including Full Run-Rate Synergies in 2009

Free Cash Flow In Year 3 To Be ~$1B

	Year 1	Year 2	Year 3
Annual Cost Synergies ($M)	$125	$250	$350
Pro Forma GAAP EPS Accretion ($ per Fully Diluted Share)	($3.25) – ($3.00)	$0.25 – $0.35	$0.95 – $1.05
Pro Forma Adjusted EPS Accretion ($ per Fully Diluted Share)	($0.45) – ($0.20)	$0.50 – $0.60	$1.05 – $1.15
Pro Forma Cash EPS Accretion ($ per Fully Diluted Share)	($0.05) – $0.20	$0.90 – $1.00	$1.40 – $1.50

GAAP EPS → Adjusted EPS

- Costs To Achieve Synergies (Yr 1 - $330M, Yr2 - $50M, Yr3 - $20M) — $400M
- Non-Cash Inventory Charge (Yr 1 Only) — $200M
- Transaction/Other Expense (Yr 1 Only) — $70M

Adjusted EPS → Cash EPS

- Annual Additional Pre-Tax Intangible Amortization — ~$80-90M

Highly Accretive Transaction Results In Approximately $5.00 Of EPS In Year 3

Source: The Stanley Works, "A Powerful Legacy, a Future of Growth," US SEC Form 8-K Filing, November 3, 2009, p. 19.