

ILLINOIS TOOL WORKS INC
Form 10-K
February 13, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

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

For the fiscal year ended December 31, 2014
OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____
Commission file number 1-4797
ILLINOIS TOOL WORKS INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware 36-1258310
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

155 Harlem Avenue, Glenview, Illinois 60025
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (847) 724-7500

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock	New York Stock Exchange
1.75% Euro Notes due 2022	New York Stock Exchange
3.00% Euro Notes due 2034	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2014 was approximately \$28.2 billion based on the New York Stock Exchange closing sales price as of June 30, 2014.

Shares of Common Stock outstanding at January 31, 2015: 379,447,026.

Documents Incorporated by Reference

Portions of the 2015 Proxy Statement for Annual Meeting of Stockholders to be held on May 8, 2015. Part III

Table of Contents

PART I		
Item 1.	Business	<u>3</u>
Item 1A.	Risk Factors	<u>10</u>
Item 1B.	Unresolved Staff Comments	<u>14</u>
Item 2.	Properties	<u>14</u>
Item 3.	Legal Proceedings	<u>14</u>
Item 4.	Mine Safety Disclosures	<u>14</u>
PART II		
Item 5.	Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	<u>15</u>
Item 6.	Selected Financial Data	<u>16</u>
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>17</u>
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	<u>42</u>
Item 8.	Financial Statements and Supplementary Data	<u>43</u>
Item 9.	Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	<u>78</u>
Item 9A.	Controls and Procedures	<u>78</u>
Item 9B.	Other Information	<u>78</u>
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	<u>79</u>
Item 11.	Executive Compensation	<u>79</u>
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	<u>79</u>
Item 13.	Certain Relationships and Related Transactions, and Director Independence	<u>79</u>
Item 14.	Principal Accounting Fees and Services	<u>79</u>
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	<u>80</u>
	Signatures	<u>81</u>
	Exhibit Index	<u>82</u>

PART I

ITEM 1. Business

General

Illinois Tool Works Inc. (the "Company" or "ITW") was founded in 1912 and incorporated in 1915. The Company's ticker symbol is ITW. The Company is a global manufacturer of a diversified range of industrial products and equipment with approximately 90 divisions in 57 countries. As of December 31, 2014, the Company employed approximately 49,000 persons.

The Company's operations are organized and managed based on similar product offerings and similar end markets, and are reported to senior management as the following seven segments: Automotive OEM; Test & Measurement and Electronics; Food Equipment; Polymers & Fluids; Welding; Construction Products; and Specialty Products. The following is a description of the Company's seven segments:

Automotive OEM: Businesses in this segment produce components and fasteners for automotive-related applications.

In the Automotive OEM segment, products and services include:

• plastic and metal components, fasteners and assemblies for automobiles, light trucks, and other industrial uses.

Test & Measurement and Electronics: Businesses in this segment produce equipment, consumables, and related software for testing and measuring of materials and structures, as well as equipment and consumables used in the production of electronic subassemblies and microelectronics.

In the Test & Measurement and Electronics segment, products include:

• equipment, consumables, and related software for testing and measuring of materials, structures, gases and fluids;

• electronic assembly equipment and related consumable solder materials;

• electronic components and component packaging;

• static control equipment and consumables used for contamination control in clean room environments; and

• pressure sensitive adhesives and components for telecommunications, electronics, medical and transportation applications.

Food Equipment: Businesses in this segment produce commercial food equipment and provide related service.

In the Food Equipment segment, products and services include:

• warewashing equipment;

• cooking equipment, including ovens, ranges and broilers;

• refrigeration equipment, including refrigerators, freezers and prep tables;

• food processing equipment, including slicers, mixers and scales;

• kitchen exhaust, ventilation and pollution control systems; and

• food equipment service, maintenance and repair.

Polymers & Fluids: Businesses in this segment produce adhesives, sealants, lubrication and cutting fluids, janitorial and hygiene products, and fluids and polymers for auto aftermarket maintenance and appearance.

In the Polymers & Fluids segment, products include:

• adhesives for industrial, construction and consumer purposes;

- chemical fluids which clean or add lubrication to machines;
- epoxy and resin-based coating products for industrial applications;
- hand wipes and cleaners for industrial applications;
- fluids, polymers and other supplies for auto aftermarket maintenance and appearance;
- fillers and putties for auto body repair; and
- polyester coatings and patch and repair products for the marine industry.

Welding: Businesses in this segment produce arc welding equipment, consumables and accessories for a wide array of industrial and commercial applications.

In the Welding segment, products include:

- arc welding equipment;
- metal arc welding consumables and related accessories; and
- metal jacketing and other insulation products.

Construction Products: Businesses in this segment produce construction fastening systems and truss products.

In the Construction Products segment, products include:

- fasteners and related fastening tools for wood and metal applications;
- anchors, fasteners and related tools for concrete applications;
- metal plate truss components and related equipment and software; and
- packaged hardware, fasteners, anchors and other products for retail.

Specialty Products: Diversified businesses in this segment produce beverage packaging equipment and consumables, product coding and marking equipment and consumables, and appliance components and fasteners.

In the Specialty Products segment, products include:

- line integration, conveyor systems and line automation for the food and beverage industries;
- plastic consumables that multi-pack cans and bottles and related equipment;
- foil, film and related equipment used to decorate consumer products;
- product coding and marking equipment and related consumables;
- plastic and metal fasteners and components for appliances;
- airport ground support equipment; and
- components for medical devices.

The information set forth below is applicable to all segments of the Company unless otherwise noted.

Enterprise Strategy

In 2012, the Company embarked on an Enterprise Strategy with the objective of fully leveraging ITW's core capabilities to deliver strong financial performance. ITW's Enterprise Strategy is centered on three key initiatives - portfolio management, business structure simplification, and strategic sourcing. These enterprise initiatives are expected to enhance the business through 2017 and are targeted at expanding organic revenue growth and improving profitability and returns.

The foundation of this strategy is a set of business practices referred to as the ITW Business Model consisting of three core elements:

80/20 Business Process - The concept of the 80/20 business process is to focus on what is most important (the 20% of the items which account for 80% of the value) and to spend less time and resources on the less important (the 80% of the items which account for 20% of the value). The Company uses this 80/20 business process to simplify and focus on the key drivers of business profitability, and as a result, reduces complexity that often creates unnecessary expense and disguises what is truly important. The Company utilizes the 80/20 process in all aspects of its business. Common applications of the 80/20 business process include:

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Simplifying product lines by reducing the number of products offered by combining the features of similar products, outsourcing products or eliminating low-value products.

Segmenting the customer base by focusing on the 80/20 customers separately and finding alternative ways to serve the 20/80 customers.

Simplifying the supplier base by partnering with 80/20 suppliers and reducing the number of 20/80 suppliers.

Designing business processes, systems and measurements around the 80/20 activities.

The result of the application of this 80/20 business process is that the Company has over time improved its long-term operating and financial performance. These 80/20 efforts can result in restructuring projects that reduce costs, and improve profitability and returns.

Customer-Back Innovation - ITW's customer-back approach to innovation builds on the Company's 80/20 business process to help ITW businesses focus on the most profitable customers and invent solutions to solve their specific problems. ITW businesses are focused on building relationships with these major customers to develop deep knowledge and insight around their needs. These customer insights and learnings drive innovation at ITW. The Company actively protects its innovation through a patent portfolio of approximately 10,000 active patents.

Decentralized Entrepreneurial Culture - ITW businesses have significant flexibility within the framework of the ITW Business Model to customize their approach in order to best serve their customers. This leads to a focused and simple organizational structure that can deliver operational excellence adapted to their customers and end markets.

Key Initiatives

ITW's Enterprise Strategy is centered on three key initiatives - portfolio management, business structure simplification, and strategic sourcing. These enterprise initiatives are expected to enhance the business through 2017 and are targeted at expanding organic revenue growth and improving profitability and returns.

Portfolio Management - The Company's portfolio management initiative aims to construct a business portfolio that leverages the Company's differentiated business model and growth potential. As part of this initiative, the Company reviews its operations for businesses that may no longer be aligned with its long-term objectives. As a result, the Company's divestiture activity increased in 2012, 2013 and 2014. With the sale of the Company's former Industrial Packaging segment on May 1, 2014, the divestiture element of the Company's portfolio management initiative is essentially complete. The Company has historically acquired businesses with complementary products and services as well as larger acquisitions that represent potential new platforms. Going forward, the Company will emphasize organic growth, while acquisitions will be targeted to bolt-on acquisitions that support and accelerate organic growth in existing segments, and new platforms that expand the Company's long-term growth and earnings potential. Refer to the Discontinued Operations note in Item 8 - Financial Statements and Supplementary Data for discussion of the Company's discontinued operations.

Another key aspect of the portfolio management initiative is the focus on product line and customer base simplification. Product line and customer base simplification focuses on eliminating the complexity and overhead costs associated with smaller product lines and customers, and focuses businesses on supporting and growing their largest customers and product lines. Product line and customer base simplification is a core element of the Company's 80/20 business process. In the short-term, product line and customer base simplification may result in a decrease in revenue and overhead costs while improving operating margin. Over the long-term, product line and customer base simplification results in growth in revenue, profitability and returns, and is key to improving the Company's long-term operating and financial performance.

Business Structure Simplification - The business structure simplification initiative simplifies the Company's organizational model and adds scale to the Company's operating divisions in order to increase organic revenue growth, enhance global competitiveness and drive operational efficiencies. This initiative focuses on reducing the number of the Company's operating divisions and increasing the average revenue size of each division, while retaining the positive attributes of a decentralized operating model. The Company expects to enhance its profitability and returns through a combination of applying its 80/20 business process to the new divisions, more focused growth investments and reduced infrastructure.

Strategic Sourcing - The Company's strategic sourcing initiative focuses on building sourcing capability in order to leverage purchasing scale to enhance profitability and global competitiveness. It incorporates both enterprise-level and segment-level purchasing that cross the Company's many businesses.

Divestiture of Majority Interest in Former Decorative Surfaces Segment

On October 31, 2012, the Company divested a 51% majority interest in the Decorative Surfaces segment. Accordingly, the Company ceased consolidating the results of the Decorative Surfaces segment as of October 31, 2012 and now reports its 49% ownership interest using the equity method of accounting. Due to the Company's continuing involvement through its 49% interest, the historical operating results of Decorative Surfaces are presented in continuing operations. Effective November 1, 2012, Decorative Surfaces was no longer a reportable segment of the Company. See the Divestiture of Majority Interest in Former Decorative Surfaces Segment note in Item 8. Financial Statements and Supplementary Data for further discussion of this transaction.

The Decorative Surfaces business produces decorative high-pressure laminate surfacing materials for furniture, office and retail space, countertops, worktops and other applications. Principal end markets served include commercial, renovation and residential construction.

Divestiture of the Industrial Packaging Segment

In February 2013, the Company announced that it was initiating a review process to explore strategic alternatives for the Industrial Packaging segment. In September 2013, the Company's Board of Directors authorized a plan to commence a sale process for the Industrial Packaging segment. The Company classified the Industrial Packaging segment as held for sale beginning in the third quarter of 2013 and no longer presented this segment as part of its continuing operations.

On February 6, 2014, the Company announced that it had signed a definitive agreement to sell the Industrial Packaging business to The Carlyle Group for \$3.2 billion. The transaction was completed on May 1, 2014, resulting in a pre-tax gain of \$1.7 billion (\$1.1 billion after-tax) in the second quarter of 2014 which was included in Income from discontinued operations.

See the Discontinued Operations note in Item 8. Financial Statements and Supplementary Data for further discussion of this transaction.

Current Year Developments

Refer to Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Financial Information about Segments and Markets

Segment and operating results are included in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and the Segment Information note in Item 8. Financial Statements and Supplementary Data.

The principal end markets served by the Company's seven segments by percentage of revenue are as follows:

End Markets Served	Automotive OEM	Test & Measurement and Electronics	Food Equipment	Polymers & Fluids	Welding	Construction Products	Specialty Products	Total
Automotive OEM/Tiers	91	% 8	% —	% 4	% 3	% —	% —	% 19
Automotive Aftermarket	2	1	—	42	2	—	—	6
General Industrial	1	18	1	14	35	1	13	12
Food	—	—	40	—	—	—	—	6
Institutional/Restaurant	—	—	40	—	—	—	—	6
Food Service	—	3	33	1	—	—	1	6
Food & Beverage	—	1	2	2	—	—	25	4
Food Retail	—	1	—	—	—	—	—	—