SNAP-ON INCORPORATED

Moderator: Leslie Kratcoski
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Operator: Please stand by, we're about to begin. Good day, everyone, and welcome to the Snap-on Incorporated 2016 Second Quarter Results Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Leslie Kratcoski, Investor Relations. Please, go ahead, ma'am.

Leslie Kratcoski: Thanks, Tony, and good morning, everyone. Thanks for joining us today to review Snap-on's second quarter results, which are detailed in our press release issued earlier this morning.

We have on the call today Nick Pinchuk, Snap-on's Chief Executive Officer, and Aldo Pagliari, Snap-on's Chief Financial Officer. Nick will kick off our call this morning with his perspective on our performance. Aldo will then provide a more detailed review of our financial results. After Nick provides some closing thoughts, we'll take your questions.

As usual, we've provided slides to supplement our discussion. These slides can be accessed under the Downloads tab in the webcast viewer as well as on our website, snapon.com, under Investor Information. These slides will be archived on our website along with the transcript of today's call.

Any statements made during this call relative to management's expectations, estimates or beliefs, or otherwise state management's or the company's outlook, plans or projections are forward-looking statements and actual results may differ materially from those made in such statements. Additional information and the factors that could cause our results to differ materially from those in the forward-looking statements are contained in our SEC filings.

This presentation includes non-GAAP measures of financial performance, which are not meant to be considered in isolation or as a substitute for their GAAP counterparts. Additional information regarding these measures is included in our Q2 earnings release issued today, which can be found on our website.

With that said, I'll now turn the call over to Nick Pinchuk. Nick?

Nick Pinchuk: Thanks, Leslie. Good morning, everyone. I'll start this call with some of the highlights of our second quarter. I'll speak about the general environment and the trends we see, and I'll take you through some of the progress we've made. Then Aldo will move into a more detailed review of the financials.

Our second quarter was encouraging, and we believe it once again offered evidence of clear advancements along our runways for both growth and for improvement. Reported sales were up 2.4% or to $872.3 million and that included unfavorable foreign currency translation, this quarter, an impact of $10.2 million. It also reflected an incremental $5.9 million from last year's Ecotechnics acquisition.

Now, organic sales for the quarter rose 2.9%. OpCo operating margin expanded by 140 basis points and earnings per share, they reached $2.36, up 16.3% compared with the $2.03 the last year. The OpCo operating margin reached 19.1%, up from 17.7% in 2015. And that 140-basis point increase reflects the higher sales, but it also represents the power of Snap-on Value

Creation. For Financial Services, operating income grew to $49.5 million from last year's $41.4 million, combining with OpCo to drive our consolidated operating margin to 22.9%, up 180 basis points.

From an overall macro perspective, the automotive repair arena remained strong and that can be seen clearly in the businesses serving that sector, the Tools Group and the Repair Systems & Information or RS&I Group. They continued to make progress in the quarter both in and outside the United States.

The Tools Group's organic activity increased 5.8%, once again demonstrating its ability to expand on our already strong position, leveraging a stream of new products and innovative solutions, capturing more business by helping technicians keep pace with changing vehicle technologies and with the aging fleets.

In RS&I, organic gains of 5.2%, higher sales of diagnostic and repair information products to independent repair shop owners and managers, increased volumes with OEM dealerships, expanded activity in undercar equipment, and broad progress in most regions.

For the Commercial & Industrial Group - well, for Commercial & Industrial, or C&I Group, organic sales were down 2%. Results were mixed across our industrial sectors and geographies. And in critical industries, headwinds surrounding our military business remained. Spending stagnation from Washington continued in the quarter. We also witnessed ongoing inactivity within the Middle East, aviation customers delaying project work due in part to the turbulence throughout that area, that region.

That said, there were positive industrial sectors, in places like U.S. aviation and power generation, where we made progress based on our understanding of the tests, our increasing understanding of the tasks and our extending product lines that enable that work.

Also a positive for C&I, SNA Europe advanced. SNA Europe, our European hand tools business delivering positive results, broad strength across the core of Europe, in places like the UK, Germany and Spain, in a period when the word Brexit entered our vocabulary accompanied by uncertainty.

So the overall results remain positive, strength in vehicle repair, mixed performances from critical industries and advancements against the wind in Europe. Opportunities outweighing the challenges and the sales growth confirms it, and the operating income clearly demonstrated the leverage and the power of Snap-on Value Creation, our Snap-On Value Creation Processes in Safety, Quality, Customer Connection, Innovation and Rapid Continuous Improvement.

In this quarter, special note should be made of Customer Connection and Innovation, keeping pace with the aging car parc and the changing technologies across the workplaces of the world.

And another broad trend, as we move toward more “automatic control” and more “drive-by-wire”, is the growing need for more precision in mechanical adjustments and more insight into data trends. Snap-on innovation is responding to that opportunity and the products that support the need for precision and insight helped drive our sales and our margins in the quarter.

Customer Connection and Innovation and in fact all of the Snap-on Value Creation Processes helped us advance down our runways for improvement everyday, driving our 140-basis point OI gain and overcoming the challenges. So that’s the overview. That’s the macro overview.

Now, let’s turn to the groups, let’s move to the groups. We’ll start with C&I. As I just said, a 2% organic sales decrease with lower critical industry activity and higher volume at SNA Europe and our Asia/Pacific and Power Tools operations. The operating income margin was 13.8%, a 50-

basis point decrease impacted principally by the reduced sales in the higher-margin critical industry business.

For the Industrial division, we had headwinds, but as we said, we also had sectors of growth. U.S. aviation sales were higher, bolstered by innovative new products like our latest in tool control solutions, the Automated Tool Control locker. You may remember, our ATC "smart" tool boxes, visually keeping track of workplace hand tools. Well, the new ATC locker brings that asset control to irregularly shaped items, like extension cords, tool kits in plastic or fabric carrying cases, personal protective equipment, all common in aviation shops. The new ATC locker makes tracking those non-standard tools easy and reliable

And like the "smart" box, the ATC locker is fully networkable. It enables tracking from a central site, displaying the tool control status for easy surveillance and avoidance of foreign object damage. Avoiding foreign object damage, a really important feature in those critical aviation applications; we can all relate to that. And based on the early reception, we believe we have a winning extension to our flagship tool control line with this locker, doing well.

Now, we often speak about customer connection, direct observation of the work and guiding new product innovation based on that observation. Well the Industrial division is constantly introducing new products, born out of that value creating process.

One example is our SGDE series of Electrostatic Dissipative screwdrivers, great for places like avionics maintenance shops or any critical application where static discharge can damage sensitive equipment. Special conductivity to dissipate static and a rotating handle mechanism that's ideal for precise, detailed electronics work. Safety and precision, two special needs made clear by direct observations at aviation MRO backshops across the world, customer connection in action, making work easier in the aviation sector, that's what these screwdrivers are.

Another customer connection, this time the Offset Crowfoot adaptor for the specially configured fasteners at power generation sites. It replaces homemade welding tools that frequently break and damage those high-voltage insulators - we've all see them on the top of transformers - damage that equals critical failure.

Visiting those substations, observing the work, we also saw Frankenstein-like modified tools, welded out of multiple tools, trying to do the transformer task and we knew we could do better. So we designed a Snap-on professional tool, that's more durable, safer and easier to use. It's a great attraction in power generation and its products like that, that are behind this quarter's positive results in that sector.

Now, let's speak about SNA Europe. During the double-dip in Europe, we said we would use RCI energetically and we did. But we also said we wouldn't reduce capacity. Well, that faith is paying-off. SNA Europe registered its 11th straight quarter of year-over-year sales growth, a positive trend in a very uncertain economic environment of Europe. And profit, Q2 marked the 13th straight quarter of margin improvement. SNA Europe up again in sales and in profit.

Our Asia/Pacific operations also contributed positively and we kept investing in that region, more products, more distribution, more capabilities, positioning to take advantage of that building potential. Well, that's the C&I story, turbulence in certain critical industries partially offset by progress in other divisions.

Now, let's move to the Tools Group. Organic sales were up 5.8%, reflecting mid-single digit gains in the U.S. and internationally. Operating margin of 18.3%, up 120 basis points, overcoming 80 basis points of unfavorable currency. That 18.3% and 120-basis point rise, it's a clear demonstration of our improving position and progress along one of our most important runways for growth, enhancing the van channel.

The advancements are evident in the sales and in the margins, and perhaps most importantly in the overall franchisee health metrics, which are all trending positively again this quarter. We believe our franchisees are growing stronger armed with an array of innovative products. Products like the new 1/4-inch Drive Extra Long Flex Head Ratchet. At 10.5 inches, it allows technicians to work in difficult-to-reach spots under the dash, in tight engine compartments or anywhere that access is limited, and it combines our patented dual pawl system with a finely machined 72-tooth gear, more power in less lateral space at a distance.

It's manufactured in Elizabethton, Tennessee, in our Elizabethton, Tennessee tool plant, and it's the next in a series of extra-long handled tools, designed specifically to make the technicians toughest jobs much easier and we believe it does just that. And early sales have been robust.

Now, we've been making torque products for some time and in the second quarter we launched the Heavy Duty ½ inch drive Mechanical torque wrench. We call it the Brutus, the Brutus 300, targeted at technicians servicing larger vehicles. It solves a critical need, making it possible to torque a wide range of fasteners using a single tool in places where a number of special tools would normally be required.

Today, the trend I described, many larger vehicles, large SUVs and pickup trucks, responding to the need for more precise specifications require a wider range of torque, some in tight places, some on buried components, some above 250-foot pounds, big components like brake calipers, pitman arms, and wheel hubs. Previously, a technician would go through a time consuming multi-tool procedure or sometimes just torque by judgment. The Brutus uses Snap-on's unique metallurgical capability to reach in the farthest places, fit in the smallest spaces, but have the strength necessary for larger torque values, all in a relatively light package for less fatigue. It's manufactured at our plant in City of Industry, California. It's long, small, light and strong, responding to a growing need for precise torqueing in larger vehicles.

Along with the innovative product, the Tools Group has another special advantage, our Financial Services arm, Snap-on Credit, strategic program aimed at supporting those essential big ticket purchases. The credit company is focused on enhancing our van network and again this quarter it did just that. So that's the Tools Group. New products, guided by customer connection, driving sales growth and strong margins.

Now onto RSI, solid across the group, organic sales growth of $14.2 million or 5.2%, operating margin 25.2%, rising 80 basis points, broad-based progress, operation-by-operation. The diagnostics and information businesses selling to independent repair shops driven by our award-winning handheld diagnostics products and by our extensive database of repair solutions.

Whether it's the top of the line, VERUS Edge with its comprehensive diagnostics, technical service bulletins, and the power of SureTrack big repair data for advanced professionals and working on those really difficult repair, whether it's that big VERUS Edge for advanced professionals or for the entry-level technician, the ETHOS Tech with its considerable functionality and attractive price point, the Snap-on line-up of handhelds makes work easier across the garage.

Some of today's vehicles now have over 100 electronic control units, all requiring service, so the demand for diagnostic tools and data insight is rising. And to support those growing complexities, our Mitchell 1 team continues to refine its ProDemand product, expanding make and model coverage, adding the most recent vehicle platforms, broadening search results, improving navigation, providing even more shortcuts to a quick fix with its SureTrack Big Database, all of it saving the technician's time. The Mitchell 1 solution gets better every quarter, and we see it in the results.

And sales of undercar equipment, also up mid-single digits with growth registered in the U.S. and our international markets.

The U.S. gains included a particular strength by a pair of RS&I's recent acquisitions, Challenger Lifts, and Pro-Cut break lathes, both expanding the Snap-on presence in the garage, and both progressing well in the quarter with products like Challenger's versatile CL12 Lift, 3-stage low profile arms for more flexibility, and Pro-Cut's new X9 on-car brake lathe, more precision in rotor matching, more repeatability of - stays calibrated over thousands of cuts. The trend in vehicle repair, more precision, that means more wheel alignment and more rotor matching and Snap-on has the products that make it easier.

Speaking about hit products and alignments, last quarter, I mentioned the launch of the V3300 Wheel Aligner. I said it was a game-changer, and so it was. Based on the enthusiastic reception from many prominent dealer networks, now with the full quarter in the book, the results are in and the sales have been strong, and it's no wonder.

We've spoken about the trend to more precision and that means more frequent alignments, enabling some of the new features like lane departure systems or adaptive cruise control and the V3300 fits that trend. More alignments are in the future and the speed and the accuracy of the V3300 is a great asset.

So to wrap-up RS&I, we see it as a confirmation together with the Tools Group of the strength of the auto repair market. RS&I great diagnostics, new repair information and expanded offerings of undercar equipment, all driving positive trends and improving our position with repair shop owners and managers.

Well, that's the highlights of the quarter. Growth and improvement. Progress, along our runways for coherent growth and clear advancements down our runways for improvement. When you step back and you look at these numbers, sales increasing organically by 2.9%; OpCo operating

income margin of 19.1%, up 140 basis points; EPS $2.36 in the quarter, 16.3% higher than last year, it was another encouraging quarter.

Now, I'll turn the call over to Aldo. Aldo?

Aldo Pagliari: Thanks, Nick. Our second quarter consolidated operating results are summarized on slide 6. Net sales of $872.3 million were up 2.4% including $10.2 million of unfavorable foreign currency translation and $5.9 million of acquisition-related sales.

Excluding foreign currency translation and acquisition-related sales, organic sales increased 2.9%, primarily reflecting higher sales in our businesses serving automotive repair, partially offset by lower sales to critical industries in our C&I segment. Due to the strengthening of the US dollar, foreign currency movements adversely impacted our Q2 sales comparisons by 120 basis points.

Consolidated gross margin of 49.4% improved 20 basis points from 2015 levels as benefits from higher sales and savings from RCI initiatives were partially offset by 40 basis points of unfavorable foreign currency effects.

Operating expenses of $264.9 million yielded an operating expense margin of 30.3% in the quarter, an improvement of 120 basis points from 31.5% last year, primarily due to benefits from sales volume leverage and savings from RCI initiatives, as well as lower stock-based mark-to-market compensation and other expenses, and a lower pension expense.

As a result of these factors, operating earnings from Financial Services of $166.4 million, including $6.1 million of unfavorable foreign currency effects, increased 10.3% as compared to prior year, and as a percentage of sales, increased 140 basis points to 19.1%.

Financial Services revenues of $69.3 million in the quarter increased 18.1% from 2015 levels and operating earnings of $49.5 million increased 19.6%. These increases primarily reflect the continued growth of the Financial Services portfolio.

Consolidated operating earnings of $215.9 million, including $6.4 million of unfavorable foreign currency effects, increased 12.3%; and the operating margin of 22.9%, increased 180 basis points from 21.1% a year ago.

Our second quarter effective income tax rate of 31% compared to 32% last year. For the full year, we continue to anticipate that our 2016 effective income tax rate will be comparable to our full-year 2015 rate of 31.7%. Finally, net earnings of $140.1 million or $2.36 per share, increased $20.1 million or $0.33 per share from 2015 levels, representing a 16.3% increase in diluted earnings per share.

Now, let's turn to our segment results. Starting with the Commercial & Industrial, or C&I Group, on slide 7, sales of $285.7 million in the second quarter decreased 3.4%, excluding $4.2 million of unfavorable foreign currency translation, organic sales declined 2%, primarily due to a double-digit decline in sales to customers in critical industries, largely in the military and international aerospace market segments.

This decline was partially offset, by mid-single digit increases in the segment's Asia/Pacific and power tools operations and a low-single digit gain in the segment's European-based hand tools business.

Gross profit in the C&I Group of $111.4 million compared to $112.9 million last year. The gross margin of 39% increased 80 basis points, mostly due to savings from RCI and other cost reduction initiatives.

Operating expenses of $72.1 million in the quarter compared to $70.7 million last year. The operating expense margin of 25.2% increased 130 basis points from 23.9% last year, primarily as a result of unfavorable sales volume leverage and 70 basis points of higher cost including cost associated with continued expansion initiatives in Asia.

As a result of these factors, operating earnings for the C&I segment of $39.3 million, including $1 million of unfavorable foreign currency effects, decreased $2.9 million from 2015 levels and the operating margin of 13.8% compared to 14.3% last year.

Turning now to slide 8. Second quarter sales on the Snap-on Tools Group of $416.7 million increased 4.5%. Excluding $4.7 million of unfavorable foreign currency translation, organic sales increased $22.7 million or 5.8%, reflecting similar gains in both the company's US and international franchise operations. Gross profit of $182.1 million compared to $176.5 million last year. The gross margin of 43.7% decreased 60 basis points, largely due to 80 basis points of unfavorable foreign currency effects.

Operating expenses of $105.8 million in the quarter compared to $108.5 million last year. The operating expense margin of $25.4% improved 180 basis points primarily due to sales volume leverage and savings from RCI initiatives and 20 basis points of lower stock-based cost associated with the company's franchisee stock purchase program.

As a result of these factors, operating earnings for the Snap-on Tools Group of $76.3 million, including $4.1 million of unfavorable foreign currency effects, increased $8.3 million and the operating margin of 18.3% improved 120 basis points from 17.1% last year.

Turning to the Repair Systems & Information, or RS&I Group, shown on slide 9. Second quarter sales of $295.2 million increased 6.4% from 2015 levels, excluding $5.9 million of acquisition-related sales and $2.3 million of unfavorable foreign currency translation, organic sales increased

5.2%. The organic sales increase reflects a mid-single digit gain in sales of diagnostic and repair information products to independent repair shop owners and managers, as well as mid-single digit gains in both sales of undercar equipment and sales to OEM dealerships.

Gross profit of $137.8 million compared to $129.6 million last year. Gross margin was 46.7% in both periods.

Operating expenses of $63.3 million in the quarter compared to $61.9 million last year. The operating expense margin of 21.5% improved 80 basis points, principally due to sales volume leverage and savings from RCI initiatives. Second quarter operating earnings for the RS&I Group of $74.5 million, including $1 million of unfavorable foreign currency effects, increased $6.8 million from prior-year levels and the operating margin of 25.2% improved 80 basis points from 24.4% last year.

Now, turning to slide 10, operating earnings from Financial Services of $49.5 million on revenue of $69.3 million compared to operating earnings of $41.4 million on revenue of $58.7 million last year. The average yield on finance receivables of 17.9% in the quarter compared to 17.8% last year. And the average yield on contract receivables of 9.3% in the quarter compared to 9.4% last year. Originations of $281 million increased 10.9% from 2015.

Moving to slide 11, our quarter-end balance sheet includes approximately $1.7 billion of gross financing receivables, including $1.5 billion from our US operation. Approximately 82% of our US financing portfolio relates to extended credit loans to technicians. In the first half of 2016, our worldwide Financial Services portfolio grew $121.3 million. As for finance portfolio loans and delinquency trends, these continue to be in line with our expectations.

Now, turning to slide 12. Cash provided by operations of $162.1 million in the quarter, increased $1.8 million from comparable 2015 levels. This higher net earnings and improvement in working

investment were largely offset by the timing of cash tax payments. Net cash used by investing activities of $95.3 million included $76.9 million to fund the net increase in finance receivables. Capital expenditures of $20.6 million in the quarter compared with $27.7 million last year.

Turning to slide 13, days sales outstanding for trade receivables of 60 days was unchanged from 2015 year-end levels. Inventories increased $9.3 million from 2015 year-end levels, mainly to support continued higher customer demand and new product introductions. On a trailing 12-month basis, inventory turns of 3.4 turns compared with 3.5 turns at 2015 year-end.

Our quarter-end tax position of $119.9 million increased $27.1 million from 2015 year-end levels. The net increase includes $341.4 million of cash from collections of finance receivables and $303.7 million of cash from operations. These cash increases were largely offset by the funding of $475.1 million of new finance receivables, dividend payments of $70.9 million, the repurchase of 377,000 shares for $58.5 million and $40.1 million for capital expenditures. Our net debt to capital ratio of 23% compared with 24.6% at 2015 year-end.

In addition to our $119.9 million of cash and expected cash flow from operations, we have more than $700 million in available credit facilities and our current short-term credit ratings allow us to access the commercial paper markets. As of second quarter-end, we had no commercial paper borrowings outstanding.

This concludes my remarks on our second quarter performance. With that, I'll now turn the call over to Nick for his closing thoughts. Nick?

Nick Pinchuk: Thanks, Aldo. Well, that's the Snap-on second quarter; continuing the trend of positive performance with ongoing year-over-year gains, runways for growth, enhancing the van channel, and expanding with repair shop owners and managers. Vehicle repair, a space with strong

tailwinds, aging car parcs, changing technologies and a need for more precision, abundant opportunity, and you can see it in the results.

The Tools Group growing 5.8% organically and an OI margin of 18.3%, up 120 basis points. Something we haven't seen. And it was achieved against 80 basis points of unfavorable currency. RS&I in the vehicle repair space, broad gains, growing at 5.2% organically. OI margins of 25.2%, up 80 basis points. Tools and RS&I up again, clear evidence that vehicle repair is strong and it has abundant opportunity and that Snap-on knows how to take full advantage.

C&I, battling the difficulties in the military and international aviation, but proving it can extend and advance in sectors like U.S. aviation, power generation and in geographies like Europe where our efforts with SNA Europe are paying off, and all of it combined to author organic growth at 2.9%.

The second quarter also bears the mark of Snap-on Value Creation, customer connection and innovation, creating a growing list of new products to provide higher value, matching the needs for greater precision and performing the work of today and of tomorrow. And RCI, people all over the corporation getting up every day and making our complex business more efficient. Snap-on Value Creation drove our OpCo operating margin to 19.1%.

Again, stepping back and looking at the performance and at the numbers, growth up 2.9% organically, performance OpCo operating margin of 19.1% up 140 basis points, a significant rise again this quarter. And EPS of $2.36, a 16.3% increase. It was another encouraging quarter. And we believe that we have the abundant opportunity and the demonstrated capability to continue that positive trend on through the remainder of 2016 and well beyond.

Before I turn the call over to the operator for questions, I'll directly speak to our franchisees and associates. I know that many of you are once again listening to this call. The encouraging results of this quarter reflect the special capability, energy and dedication you bring to our effort every

day. For your clear achievement in this period, you have my congratulations and for your contributions and your commitment to our team, unfailing, you have my thanks.

Now, I'll turn the call over to the operator. Operator?

Operator: Thank you, sir. If you'd like to ask a question, please signal by pressing star 1 on your telephone keypad. Please make sure your mute function is turned off to allow your signal to reach our equipment. Once again that is star 1 to ask a question. And we'll go first to Scott Stember with C.L. King.

Scott Stember: Good morning.

Nick Pinchuk: Good morning.

Scott Stember: Could you maybe just talk about the overall industry backdrop for the automotive aftermarket, doesn't seem to have that much of an impact on your quarter, but just, you know, specific to whether you saw any, you know, mechanics or, you know, end-markets that were backing off on tool purchases, you know, somewhat in the quarter?

Nick Pinchuk: Not really. I mean, I think, look - I think, every quarter is different and there are ups and downs in every quarter in terms of the growth and in terms of the types of products that sell and so on, big ticket was very strong. I was just on a van within - just a little over a week ago and the franchisees and the garages we visited were all very, very optimistic. So I didn't get any feeling from that, from an anecdotal point of view.

And then, you know, during the quarter, I met with our - a group of our franchisees several times from the United States and Canada and so on and they seemed uniformly positive. And when I look at the numbers, you know, I think this market looks like it has looked to us for multiple

quarters now, for a long time. So empirically with the numbers and anecdotally from what I get from talking to franchisees and technicians, I think this is pretty positive.

Scott Stember: Okay. And focusing on the Tools Group, maybe just talk about some of the, you know, higher-priced electronics versus, you know, traditional tools and power tools, maybe how that, you know, trended in the quarter?

Nick Pinchuk: Yes. Well, big ticket items. What we've - diagnostic sales were strong in the quarter, you know, for the Tools Group. You know, we - you have kind of a secular trend in the market, what I characterized in my remarks as a tailwind, the need for more diagnostics because, you know, 40% to 50% of repairs in the parc today need a diagnostic to effect it efficiently and new cars are 80%, so there is a growth toward everybody needing a diagnostic, we see that in our everyday sales and the trends in the market. But in this particular quarter, big ticket items were fairly strong, high value, some of the things I talked about high-value tools that attack precision like the Brutus 300, strong-seller.

So the idea - hand tools in fact were also up very strong. So we saw I think pretty wide strength, but again in this quarter, big ticket led the way. And that's what we expect, because our marketing gains around Rock N' Roll Cabs, and we've just done a major refurb on the TechKnow vans, have kind of supported those purchases.

Scott Stember: Got it. And just last question on currency, you know, when you would expect to start to see some of the easier comparisons with the...

(Crosstalk)

Nick Pinchuk: For your information, you know, for example, you can look at it this way. In the second quarter, the numbers were in sales, we had about $16 million and 9 cents of currency impact

between transaction and translation. In this quarter, we had $10 million and 7 cents, you know, $10 million - just north of $10 million in currency and in sales, I think that's 1.2% or something like that and about 7 cents of currency impact on profitability, 50 basis points in the OI, impacting the OI margin.

If you go forward, if everything stayed where it is, you know, for us the pound is a big - is kind of a big deal. So I think you would say that in the third quarter, the comparisons are such that there would be a slight easing if everything stayed the way it was and then the fourth quarter would get easier I think for us, so that's the way we'd see the year going on, an easing of the pressure of currency, but I think that happens more in the fourth quarter and the third quarter, primarily because of the pound and the pound does carry uncertainty around the exchange rate today and anyway in that situation. But if it stays the way it is today, that's how it'll be.

Scott Stember: Okay. And just a quick follow-up, sales that are, you know, bound by the pound, what percentage of your total sales are coming from that region?

Nick Pinchuk: About 8%...8% or 9%...About 8% or so. And, you know, no one knows what the - what Brexit is going to do. You know, the roll up to Brexit was I think a time of uncertainty. We didn't really see much change, but, you know, we're selling into a very basic critical industry, so our people are going to - I think our people buy. We've even see it. So on a deep recession, people bought the small - the low payback - the short payback items, even in the deepest of recession. So it remains to be seen what effect Brexit will have, but we're optimistic about it. Okay?

Scott Stember: Got you. Thanks for taking my questions.

Nick Pinchuk: Sure.

Operator: If you find that your question has been answered you may remove yourself from the queue by pressing star 2 at any time. Again star 1 to signal. Next to Gary Prestopino with Barrington Research.

Gary Prestopino: Hey, good morning, everyone.

Nick Pinchuk: Good morning, Gary.

Aldo Pagliari: Good morning, Gary.

Gary Prestopino: Nick, what - you didn't give a percentage on the European hand tools up in the quarter, can you share that with us, or maybe I missed it?

Nick Pinchuk: It was up low-single digits in the quarter.

Gary Prestopino: Okay.

Nick Pinchuk: So we usually don't give percentages, you know, but we have given it in those kinds of terms, mid-single digits, low-single digits, high-single digits.

Gary Prestopino: Right.

Nick Pinchuk: It was up more in profitability. You know, we're pretty encouraged by that though. Like I said, it's the 13th straight quarter growth. And what's really encouraging I think is the growth in core Europe. We haven't seen growth in the core of Europe like this before uniformly. So I am a little encouraged by UK, Germany and places like that. France, it was encouraging for SNA Europe.

Gary Prestopino: And then, the previous caller asked a question about currency. Did you say that currency comparisons for the pound should get easier as we go through the back half of the year?

Nick Pinchuk: I said - what I said, well, hard to predict, you know. I mean, the thing is - and you got the cocktail of what you sell and all that stuff. But if all things remain equal, what will happen is, is that currency in general will get - currency in general, the pound becomes more difficult I think as you rollout through the year, but then the other currencies abate.

So if you look at the total, it gets - if everything stays the way it is, and the mix stays the way it is, you end up having a little softening in the third quarter and more softening in the fourth quarter. I think that's the way to think about it.

Gary Prestopino: Okay.

(Crosstalk)

Nick Pinchuk: ...problematic and in fact it might be...

(Crosstalk)

Gary Prestopino: Right. So would be the Canadian dollar and the euro...

Nick Pinchuk: Canadian dollar, Aussie dollar, you know, the euro, the SEK...

Gary Prestopino: Right.

Nick Pinchuk: ...those kinds of - those kinds of currencies, the comparison simply get easier later.

Gary Prestopino: And then did you see any disintermediation in Europe post-Brexit for the first couple of weeks of this quarter, can you discuss that at all?

Nick Pinchuk: No. We don't comment on the forward quarter, but I don't really think so. I mean, certainly I'll say this, there was a lot of uncertainty in the - going - I was in Europe just before the Brexit vote and there was a lot of uncertainty floating around, around that and we didn't see it impact then, I don't know what will happen going forward. But again, I say, we sell items that solve critical tasks, that tends to be less affected by the economics. It can go up and down in a short period, but I think over time, it doesn't get affected. So I don't really think we expect it in that situation.

Gary Prestopino: Right.

Nick Pinchuk: If the exchange rate changes dramatically that would have a transactional effect of course. If it affects interest rates that would have another thing around other than - in other parts of the corporation, but I don't really - we didn't see anything so far.

Gary Prestopino: And then in terms of the Snap-on Credit, it keeps growing in excess of the sales of the Tools Group, are you seeing more of an appetite or are more products being financed by the technician that...

Nick Pinchuk: No, not so much. Not really that. I mean the thing is fundamentally, what's happening in the Tools Group, if you look at it from our perspective and we look at it, you can't look at any one quarter because there is a secondary market and there is a lot of - that's actually the franchisee sales not our sales, so it doesn't match up. There is a lot of noise from quarter-to-quarter. But if you look at overall the last year, the originations are roughly the same as the sales of the big ticket items. So, you know, it's being driven by the sale of those big ticket items. And if you've

been a student of Snap-on, you know that we have been energizing big ticket sales through, we think, better product of course in diagnostics and tools storage, but also in terms of the marketing, in terms of the marketing, the Rock N' Roll Cabs and the TechKnow vans. So if I didn't know anything, I would say Snap-on puts Rock N' Roll Cabs and TechKnow vans in and it makes clear coat boxes, I'm going to see higher originations because it's going to have higher big ticket sales.

Gary Prestopino: Okay. Thank you. Thank you, Nick.

Nick Pinchuk: Sure.

Operator: We'll go next to David MacGregor with Longbow Research.

David MacGregor: Yes. Good morning, everyone. Thanks for taking the call. Nice quarter, Nick.

Nick Pinchuk: Thank you.

David MacGregor: Just talking about the growth though in the Tools segment, you guys peaked out in the first quarter of 2015 at about 13% organic growth. And just because of the comping process, obviously that's not a sustainable level and you're going to be coming down. But that organic growth has been sort of settling back down for six consecutive quarters now; you're back to 5.8% this quarter. You talked many times in the past about the long-term growth in the Tools segment, it's probably closer to about 4%. And I just wonder, are we on our way back to that kind of level here in the second half of the year or, you know, is there something...

Nick Pinchuk: I think, what I said is - I'll say - I'll make two comments about that. One is, is that, you know, all through, you know, there has been periods when we grew at like 6% or 5%. During the string of 23 out of 24, I think a year before in 2013, I think, we grew it like - we threw a bunch of 6s during that period. So it goes up and down. There is fluctuation.

I've said this, I think - look, I think the Tools Group goes in the 4% to 5% range, you know, if based on the tailwind. It's got, that's a great market. Automotive repair is the market, in our model is one of the business models that fell from Saturn. Automotive repair is one of the great, great markets. You've got aging of the parc and you've got changing technology, you've got more precision and that will drive us in a 4% to 5% range. And things like Rock N' Roll Cab and TechKnow Express and the system program drives us up into higher levels depending on how effective that unleashes these - how much more effective that makes the van business. So from time-to-time, we get above this.

And I think our ability to grow above the 4% to 5% depends on our ability to keep coming up with those things. That doesn't mean we can grow at every quarter. So I think that's how I view it. I think we were at a solid 4% to 5%. But I think if we can keep coming up with ways to amplify our business, the technicians are there. There's 1.3 million technicians, we're calling on 850,000 of them, and a lot of them are hiring every year. So we see a great market there. The other thing I will offer about the quarter, Yes, it was 5.8% but 18.3% OI margins.

David MacGregor: The incremental margins were fantastic and you said...

(Crosstalk)

Nick Pinchuk: Try to find one of those in the Tools Group history.

David MacGregor: Yes. But...

(Crosstalk)

Nick Pinchuk: That was against 80 basis points.

David MacGregor: Right. Could you...

(Crosstalk)

Nick Pinchuk: So I guess the, you know, the less than 6% sales and 7% sales didn't affect the profit, you know, so they're still bringing the money...

David MacGregor: Right.

Nick Pinchuk: ...to the bottom line.

David MacGregor: And you've said repeatedly that, you know, during that period of, you know, superb growth that, you know, you're not too focused on costs, you're more focused on just, you know, bringing in the business. But at some point that growth would ease and that's where we would see the margin improvement, just there was a lot of low-hanging fruit.

I guess, you know, which is part of why I asked the question, and now you're starting to see the margin growth which would confirm as a milestone that, you know, maybe we're at that point where the growth starts to ease. But, you know, you also said earlier in the call that you're still seeing strong, you know, double-digit growth in originations and originations attracts big ticket. So I guess the question I would next ask is, you know, what's easing within Tools, what do you see that if big tickets are holding up, you know, what's easing on you?

Nick Pinchuk: Well, look, I didn't say in the quarter that was - I didn't match the double-digit growth of big ticket to the - or double digits of originations in the quarter, because you can't do that. You got to look at it over a longer period. So what I did say was the double digits in 2000 - of originations in 2015 matched, almost pretty close to dead-on, the growth of the big ticket items in 2015. In any

quarter, it's hard to say that. I don't think in the quarter, the more robust businesses were around diagnostics, around hand tools. I think we had a dynamite hand tool quarter, but maybe we had a possibly less of a power tools quarter than we did in the prior quarter, that's the kind of characteristic we had. So we had some goes-ins and goes-outs, if you want to look at it by product.

David MacGregor: Yes. And you're not adding any more tech or Rock N' Roll Cab Express, so I presume that the storage part of this is starting to level out a little as well, is that correct?

Nick Pinchuk: No. Yes, Yes. But we actually did add one in the quarter. So we went from 66 to 67, I mean, okay, it's not much. Look, I don't - I think it's one quarter. I'm not saying that - I'm not - we don't give any guidance, I'm just saying it's one quarter, so I think it's a little wrong to explain to view it totally as what were the mix in one quarter and, will tool storage go down, I don't think so.

David MacGregor: Okay. Last question was just you talked on the last call about extending a little more credit to your most discerning franchisees, guys with the strongest track record at dispensing credit. And I'm just wondering where did that credit get put to work in the quarter and where does that show up in the segment numbers, if in fact it did get put to work?

Nick Pinchuk: It shows up in the originations and in the Tools Group, those are the big ticket items. Those guys are wielding big ticket items. So that's part of the support system that allows us to sell those big ticket items. I mean big ticket is basically - and it has been for Tools, this has been 30 years of this or 50 years, I don't know how long, but it's been since the 1980s at least that they have been and I think longer that they've been financing big ticket items in this way.

And what we did, as you said, is - what we did was just bring striping to the franchisees where we listen more to some guys and listen less to other guys depending on the record to call in the air strikes about appropriate credit. And in the quarter, that kind of - I think in the quarter, that kind of

was relatively stable. But over like the last 18 months, we've had - we stripe more guys that have been better at credit, and they've been able to aid the credit process more effectively.

David MacGregor: All right. Thanks very much.

Nick Pinchuk: Sure.

Operator: We'll go next to Bret Jordan at Jefferies.

Bret Jordan: Hey, good morning, guys.

Nick Pinchuk: Yes, good morning.

Aldo Pagliari: Good morning.

Bret Jordan: Just to follow-up...your comment on the secondary market in the - on the credit side, I'm just sort of trying to line up the growth in the finance book relative to the growth of sales. Has anything - and I guess we've decided that there is not an increase in penetration of credit on a transactional base, so you're not lending at a higher rate. It's been more a growth of high-value sales, but then you had a comment about the secondary market sort of creating some volatility there. Is that when your lending on a transaction where a franchisee is selling a used tool they took on trade?

Nick Pinchuk: Yes. Let's take it this way. Yes, that's essentially what it is. But what I meant was, what I offered that comment for is, it's harder to take one quarter's numbers in origination and relate it from originations, the credit action to the actual sale, which is a movement of product from us, from Snap-on Tools to the franchisee. The product moves from Snap-on Tools to the franchisees, it might go into inventory, it might sell directly, and it might ignite say, okay, I've sold you this Mr.

Big Box, it's like 15-feet wide and I took your 7-foot box in trade and I'm selling that. Both transactions would be financed. And so while the net, you get a discount from the original for the amount in trade and then that would be on. So the total amount tends to be sort of the same. The timing of those two things can be very different. So a franchisee might end up in his garage, might have three boxes, used boxes waiting there, and then one quarter might roll them all out, might find a seller for them, you see what I mean. And so...

Bret Jordan: Yes, I do.

Nick Pinchuk: ...that tends to distort the timing, not the amount, but the timing.

Bret Jordan: Okay. And then back on the Tools, on the contribution from RCI versus leverage, did you discuss sort of what the RCI impact was in the prepared remarks, I didn't hear it?

Nick Pinchuk: Sure. I mean, the Tools Group is more or less like this. The OI margin is up 120 basis points and they had 80 basis points of negative currency. The principal offset is RCI.

Bret Jordan: Okay. And then one question on C&I. You talked about U.S. aviation and power generation being highlights. Did you say anything - are you seeing any shifting trends? I mean, energy was a category you used to call out as being challenged? Is there any sign of improvement in some of the other big pieces like energy or mining that have been lagging in C&I?

Nick Pinchuk: Well, you know, mining, I don't think so. Energy, generally, oil and gas is still lagging, but not by the mammoth proportions we saw in the in the first quarter and the fourth quarter of last year. You know, so that came back a little bit. That got better. And for, you know, for C&I in general, as we go into the third quarter and fourth quarter, we start to get into, I'll say less demanding comparisons in military and in international aviation as well. So you see that kind of effect going on.

In terms of the quarter-to-quarter business, we saw - I think we saw rays of hope in places like U.S. aviation and power generation. And general industry seemed to be fairly nice in the quarter. So we're encouraged by that, but I'm not - given the fact that we're down 2% in the quarter and down more in the critical industries, I'm reluctant to predict any turnaround until I actually see it.

Bret Jordan: Okay. And then one final question on RS&I, just to cover all the bases. In the mix of software versus hardware, are you seeing a shift where you've got this great penetration of diagnostics and you're selling software upgrades and that's increasing as a percentage of the mix or is that business kind of stable? It would seem like the software margin should be pretty good.

Nick Pinchuk: Software margins are pretty good, but I'd say in the quarter, it was relatively stable. From time to time, we can see a bump from software based on, you know, we'll issue 18.4, you know, will come out in a quarter and that will bump the software sales. But generally, I would say, you know, our software sales go up with the general push of diagnostics. Remember, we tend - when we're looking at RS&I, we're looking at the sales we show you have quite a bit of software in it in Mitchell 1. Mitchell 1 is a pure software business. Repair shop information and repair shop management, that's where that SureTrack business is.

Generally, though I don't think, you know, we've seen a big change in the mix yet. You might be entitled to the idea that going out future as we get more installed base, you may see some improvement in that. I tend to think as we get more installed base, we'll see both because people will buy in first. You know, the entry-level technician will buy in at the bottom level for that ETHOS. And then when he starts to, you know, get more experience, he'll want to trade up and he'll buy both software and hardware as he trades up.

Bret Jordan: Okay. So the penetration rate of hardware is still growing. It's not just...you don't have a cycle where you get to sell a lot of - a very high-margin software to a large installed base of hardware?

Nick Pinchuk: No, we eventually will. I mean, but I think now, we're still seeing a growing of the penetration.

Bret Jordan: Okay. All right. Thank you.

Nick Pinchuk: Sure.

Operator: We'll go next to David Leiker at Baird.

Joe Vruwink: Hi. Good morning. This is Joe Vruwink for David.

Nick Pinchuk: Hi. Joe.

Aldo Pagliari: Hi, Joe.

Joe Vruwink: I just want to circle back on your C&I comments. I think it was last year in Q3, when military took its first step down and then energy followed in Q4. So when you look at spending levels in those two businesses as we head into this year's Q3, do you think you could actually get to the point where the comparisons flip around and C&I reports a positive comp in Q3?

Nick Pinchuk: Well, as I said, I think the comps get easier. Clearly, the military comp gets easier, the international aviation comp gets easier, the oil and gas comp kind of is starting to get easier now. So I think those get better. Whether I can predict a turnaround in the military business, the oil and

gas business, or the Middle East loosens up, hard to say. They do loosen up and I think you see favorable comps.

I mean, like I said, I am positive about our mechanism there, our proof-of-concept. We keep investing in those businesses. If you look at the C&I SG&A or OI this quarter, you see quite a bit of investment, that's because we invested in Asia, we kept investing in these markets because we believe in them. So we obviously believe a turnaround, whether that's the third quarter or not is another question, but the comparisons do get softer.

Joe Vruwink: Great. And then shifting back to the Tools Group, not to belabor this question, but growth slowed more than two points sequentially and your comparisons versus a year-ago got easier. So by saying that hand tools were good in the quarter and big ticket items were strong in the quarter, there just seems to be a missing link in the equation that would explain why growth ultimately did decelerate?

Nick Pinchuk: Well, as I said, you know, I don't really want to go through all the items, but the power tools is down and so on. I don't necessarily recognize that the comparison was necessarily soft versus last year. I'm not really sure about that. But the thing is, is that, from our view, we're not seeing - all I can say is, we're not seeing anything in the market that's different. And so the 5.8%, Yes, it's down from the 8.1%, but we still see it as a pretty strong quarter and we don't have any other view of the future of the Tools Group or the auto repair market based on that.

In terms of how the numbers, how the numbers work out, like I said, big ticket, still strong, sold better than the average; hand tools, sold better than the average. The other ones were - obviously if you talk about arithmetic, they were lower than the average.

Joe Vruwink: Okay. Fair enough. My last question, with Fortive being its own company, Matco has been a little more visible and it looks that their van count has grown pretty dramatically in recent years,

but it doesn't really seem to be diluting Snap-on's growth at all. And so is it the case where the two of you or really the three of you in this market co-exist? Is there any deterioration or things that you're concerned about, just maybe an update on the competitive dynamics?

Nick Pinchuk: Well, the scions of Danaher are strong managers, and so Fortive is a formidable competitor with Matco and so is MAC. But, I haven't heard their names mentioned on the last several - in many, many van rides now. So - and including the last one, which was just a little while ago. So we don't seem to be seeing them impinging on them. Whatever they are doing, they are doing it invisible to most of our people. I tend to think people decide to buy Snap-on Tools as they look at others. You know, they make that choice, you know, it's kind of a binary decision. You buy Snap-on because that's the best. If you don't, if you don't, if you don't want that, you look at a bunch of others.

Generally, if you think about the numbers of people that we have in the field, the 3,487 vans and versus the - even the advanced Matco numbers, we're - our people are much more focused and spend more time with a certain amount of customers and calling on those customer bases. The Matco and MAC guys must chew a lot more dirt.

Joe Vruwink: Very good. Thank you.

Nick Pinchuk: Yes.

Operator: That concludes today's question-and-answer session. Ms. Kratcoski, I would like to turn the conference back to you for any additional or closing remarks.

Leslie Kratcoski: Thanks everyone for joining us today. A replay of the call will be available shortly on snapon.com and as always, we appreciate your interest in Snap-on. Good day.

Operator: This concludes today's conference. We would like to thank you for your participation. You may now disconnect.

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