Company Name: Snap-on Incorporated (SNA)
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<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Good afternoon. I'm David Leiker. Our next presentation is from Snap-on. This is one of our favorite business models. I've know this company for years. Over the last 10 years or so, organic revenue growth here has accelerated. We're seeing 8% type growth numbers today; even margins are in the 17% to 18% range and rising, EPS growth is 13% and keep going.

Over the last 20 years, Snap-on sales have grown in every year expect two, so recession resistant, not rescission immune. They make and sell tools, equipment, diagnostics technology for professional auto repair market, significant presence in the industrial tool market. Representing – presenting Snap-on today is Nick Pinchuk, Chairman and CEO.

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Okay. Thanks, David. Okay, I'm from Snap-on. Here is the slide. We have the cautionary slide. That's up to you to read it carefully. You'll know what we talk about. Okay. Look Snap-on, everything I say about Snap-on is not with any necessarily of pride ownership. I'm not a lifer. I've only been there 13 years and at Snap-on that is a short time. And so what I say has been accrued over much time.

Snap-on is a company that I think has tremendously innovative product line, has nonpareil quality recognized like that, has a strong brand and legions of loyal customers and despite that fact it has tremendous runways for both improvement and for growth. You can see this in our financials and we expect it to continue.

Over time, if you can think about it Snap-on was founded in 1920. It's founded – the auto industry was just starting, and the repair industry was even more, and definitely the fact was the array of tools was dizzying and here comes an engineer from Milwaukee, Wisconsin. He says he can change all that. He comes up with the idea of five handles of different dimensions, different configurations, an ellipse, a T, and so on, puts them together with 10 sockets of different dimensions and fashions them so they snap on interchangeably. It revolutionized tool sets all over this country. He said those five handles do the work of 50 tools and he was right.

He made them with the highest quality steel. And so the idea of innovation with that first tool and quality has echoed down through these more than nine decades to us. It's allowed us to keep adjusting for the changes and the mechanisms from vehicles to jet engines, to oil and gas in today, and that's what drives our business. He did something else that was really important, I love to talk about this.

He told the salesmen to go into the garage and lay the tools out on green felt as if they were precious as surgeon's knives, implying that if the mechanic used these tools, he would declare to the world that he's doing something special, perhaps as special as the surgeon, and the idea that Snap-on tools are the outward sign of pride and dignity in working men and women – for working men and women in their profession, is what's at the core of what we do today.

It's the reason why people buy our jackets and buy our 95th anniversary boxes, paying $8,000, $9,000 $10,000 for a box to put in their workplace, what is essentially a shrine to our company because they like to associate with our name, because it's the outward sign of their pride, dignity, and all of that. Since 1920, we've expanded, we're in 130 countries. We have 4,800 vans. We have more than 65,000 SKUs. We have 3.3 billion in sales, and between $9.5 billion and $10 billion of market capital. We have paid a dividend every quarter since 1939, and we have never ever reduced it, a testimony to the strength and repeatability of the model we have.

Now, here is how we're organized. We're customer facing. You see the red. That's the van business. This is what everybody thinks of when you talk about Snap-on. It's been a van business for a long time. It's been the vans for a long time, for decades. These are white vans with red Snap-on them. They go across the countryside and they call on technicians in weekly routes. Their primary customer is technicians.

Now, this is a business that calls on a customer base that's growing at 1% and yet that business grew in the quarter 11% organically and the quarter before that 11.2%, the quarter before that 12.9%, the quarter before that 11.8%, and 21 of the last 22 quarters it grew at 6% or more and the only quarter it didn't grow at 6% was Superstorm Sandy, in which it grew at 3.7%. I think abundant evidence that Snap-on is an under wielded property that has opportunity.

If you look at an aligned business, the RS&I business, 28% of our business. It's dark blue up here. It sells to repair shop owners and managers. That grew at 8.2% in the quarter organically. The yellow is the finance company, which supports the big ticket purchases at both of these places, strategically supporting it – that company's OI grew at 15.4% in the quarter. And then the light blue, the commercial and industrial group, rolling the Snap-on brand out of the garage into other industries that are critical, where repeatability and reliability justify Snap-on level premiums, and Asia-Pacific, which is an emerging market and that grew at 3.4% and its OI was up 60 basis points in the quarter. If you roll that all together for the quarter, for the last quarter, Snap-on grew at 7.3% organically. OI margin for Opco, the operating company excluding finance, was 17.5%, up a 130 basis points against 50 basis points of currency. EPS was $1.98. That was up 12.5% and it absorbed $0.15 of currency bad news.

But despite that, we think there is a lot more opportunity going. In the future, we call - we designated in two big areas: runways for growth and runways from improvement. Our runways for growth are basically doing what we've done forever for auto technicians, but doing it for some new customers. First, it's taking the van business and enhancing it. And if I would say that 11% growth and 11.2% growth and 12.9% growth are abundant evidence of that's possible. Expanding with repair shop owners and managers. These are those guys who stand right next to the technician customers, but our share isn't as big. That's the RS&I Group. That grew at 8.2%. Extending to critical industries. Rolling the Snap-on brand out of the garage. We can see our strategic trend working in that area. And building in emerging markets, I just came back from China, and we're adding more strength in that business all the time.

That's our runways for growth. Really though doing just what we always did for auto mechanics, observing the work, making it easier, coming out with solutions, and nurturing that brand or supporting that brand or taking advantage of that brand. And then on the other side, runways for improvement. Snap-on came late to process improvement, but if you look at our process improvement activities, they keep expanding, 130 basis points in the quarter.

And its focus on processes of safety, quality, customer connection, innovation and rapid continuous improvement. Safety because we make things for customer – for working men and women. We keep our own people safe. They're 92% safer than they were 10 years ago.

Quality. We used to have quality, but now we have a statistical backing to this quality. When you ask customers in repair shops across America, what's your prepared from of hand tool, 70% say Snap-on. Number two is eight. If you ask them about diagnostics, it's 63 to 67.

Customer connection and innovation, we're turning out more new products than we ever did because we're in more garages for more hours, more workplaces for more hours than anybody else. And the new technology in product development, things like 3D modeling and finite element analysis and so on, have asymmetrically enabled the complex product line, the 65,000 SKU product line that we have.

Rapid continuous improvement. Our people focus everyday on how to make things better. And the management team spends at least one week a year in a factory doing just the same thing to point out it's important; and this is why our OI margin was up like 130 basis points in the last quarter, and it was 100 basis points up the quarter before that. And we say we can increase OI margin without incremental sales because Snap-on has a lot of opportunity given the 65,000 SKUs to improve on a complex environment.

So that's Snap-on; innovative product line, strong brand, legions of loyal customers and lots of runway for both improvement and growth.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Great, great, thanks for the overview. As we go to questions here, anybody has the question put your hand up, I'll get to you or you can email, session2@rwbaird.com, I'll work them in through along the way. I want to go back a little bit in time. I mean I know that we talked about this part of your business in the last several years that that we've had this opportunity to talk, but you came to Snap-on and correct me if I'm wrong in this, but in 2002…

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Correct.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

…became CEO on 2007. Before you've got there though, this is a business that was horribly undermanaged; I think I went a decade with no revenue growth. I'm not calling you out as the catalyst for change, the structural change had happened before you took the mantle. What's behind this 10 year, 12 year, 15 year period, of fundamental change in the business and how its run today in terms of relative to how it was run in the past?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

I think is this, I'd say, we understand better today, who we are, what makes our business work, and why what are the essentials of the Snap-on business model. That is what our principle value-creating mechanism is observing work, understanding the work, and figuring out how to make it better. We know now it's not rooted in a technology or in a particular product. And I think like many companies that are successful that have had a run of a great brands and so on, sometimes we lost sight of that. And the fact that we know that now, and we understand that these certain things will help us, has allowed us to grow.

For example, the Tools Group. The Tools Group, we understand that changing our product line or coming up with new products will help excite our customer base and get them to buy more tools and solve their problems. We understand that one of the key elements of the Tools Group is that those vans are bounded by space of vans and time of the driver, and we figured out how to break through that. Those are the kinds of things that have created this runway for growth.

So the understanding of the business, the fact that Snap-on thrives by observing work and making it easier in areas of criticality where repeatability and reliability are important, have allowed us to see how to make the vans better and have allowed us to see these other opportunities in critical industries and emerging markets. That's one. And number two is we just figured out that like all mortal companies we had to pay attention to process and actually work it very hard. And so we live this very much everyday. Our people really believe in process. And if you just take a look at RCI, we have an RCI coordinator with rapid continuous improvement or lean. We have a lean coordinator in every facility, every major facility. He gets up everyday and figures out how to make things better.

We have Shingijutsu events, the Japanese consultants. We have 10 to 15 of them in our organizations throughout the operation every year in which we bring people from all over the company to sit at their feet and further our understanding of lean. And then as I said once a year the whole management team goes out and participates in this, signifying that it's very important.

And it's authored the trend of operating improvement. You said, you went back to like 2002 or 2005, our OI margin was 6.5% and then with 7.6% and 10.6% and 12.3% and 9.9% during the recession and then back to 12.1% and then 13.0%, 13.5%, 13.9%, 15.1%, 16.3% last year, and all of that's been driven by this rapid continuous improvement and Snap-on value creation.

And we believe because we make 65,000 SKUs and our product line is very vertically integrated, raw steel comes in the back and we hand the tool to the end user, how many manufacturing companies are so vertically integrated and so broadly expanded those 65,000 SKUs. This is a complex landscape in which there's lots of improvement. You'd be shocked at how many screwed up things there are still at Snap-on, and therefore we can keep improving.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Maybe took my next question away from me.

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Okay.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

One of the questions was…

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

How many screwed up things there? Many.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

One of the things – you get the questions and we get the questions from investors.

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Right.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

And you put the fantastic 10-year track record of driving revenue growth, driving margins almost year after year after year. Everyone wants to know where are you, how much room is left? Where do you think you are in that opportunity to drive revenue growth well above what the end market is doing and the ability to drive margins like?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

I'd say in terms of process we're like in the fourth inning. We have a lot more to – I'm not kidding when I say that if we never got another dollar of incremental sales, we could keep the profitability going up. I'm convinced of that. And if we can't make Snap-on margins among the best in industrial companies anywhere, we're not who we think we are. We're very confident of that.

And in terms of growth, I think the Tools Group has been around for so long, I just say, that growth in the Tools Group should be abundant evidence that Snap-on was under yielded, (I keep dropping my thing here), Snap-on was under yielded, under wielded. And so, I think there's opportunity there. And we're kind of just coming to the idea of the other customer basis: the emerging markets, the critical industries, the repair shop owners and managers. We just starting to understand what makes their work easier. And as we do, we're going to be every bit as powerful in those sectors as we are in the auto repair sector, technician sector.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

So let's take those two pieces of your business, the emerging markets, the critical industries...

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Yeah.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

They are each about 10% of your sales or so today.

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Right.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

How large – could they be 25% of your sales some day?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Well, I think, we said that the business in critical industries are, like you said, 10%, 12% of our business. That's like $450 million, $400 million, $450 million. We say it's going to $1 billion. And we only say that because these are heavy vertical markets. We don't know how far it could go. We're kind of operating in early days, just putting our foot in the water for most of those segments. Places like military we're a little stronger because when we have the idea of expanding to critical industries we said military would be probably the most critical. When the 50-caliber bullets are flying overhead, you think that's critical and you'd want to repair the vehicle. But the other ones we're just kind of starting, but what I'm encouraged about is we're starting to understand great ability to bring on products.

Last year, 996 new products in aviation, 869 in military, 658 in oil and gas, and so on. And we're on that pace this year to do that. So I see that positiveness. That's going to be $1 billion plus business. In emerging markets, it's hard to say. The time constants are hard to decide, but you don't have to be a genius to look at say China, for example. There's 150 million cars on the road in China versus say 280 million, 300 million in the United States, but in North America – North America, they're 11.5 years old; in China, they're 4.4 years old, 3 years warranty. Most of the cars are on warranty in China, so the repair wave hasn't yet started; but if you start to do the math, you see the wave starting to coming on us. And what we're doing is we're building our emerging market position, particularly in Asia. In 2004, we had nothing there. We had two offices and 10 people, now we have 5 factories, 1,500 people, a design center with over 100 engineers, 800 resellers, 11 Blue-Point shops, a number of vans. I just came back from Asia myself. I think I still have Shanghai fluids in my body and renminbi is clearly in my pocket. I was there. I just came back…

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

[Multiple Speakers] (0:17:19)

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

I guess so, yes I got to flush it out, right. And so – what – time yet the same…

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

China time…

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

China time, yes, thank you. Right, I'm on China time. Anyway, I see us having the great opportunity to grow. The time constants, I'm not so sure, but if you start to look at that and you say okay it's going to be a little slower because the Chinese don't drive as much as the Americans, but the products are aging and they're starting to get into the $25 million a year sales, are starting to age, so it's going to start to come. And the OEMs, which are now doing, the OEM facilities, what we call 4S shops, are now doing 70% of the business. They're not going to be able to handle it. It's going to flush into independent shops. This is our sweet spot, independent shops. So we're pretty positive about it.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

A handful of questions here from the audience. If we look at your pricing power, the ability to price your product, how is it priced compared to your direct competitors to what you could find at a Lowe's or Home Depot? And is there any tie of that related to the nature of the mechanic in North America's skilled labor force and that encourages them or their desire to own more expensive tools?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Lowe's or Home Depot? I think our ratio to them is, well Craftsman I know, where we have a premium over say Craftsman. So is there anybody here who is watching NFL football last night, you saw Craftsman advertisement where we have a little premium or five or six times of Craftsman. I don't mean 50%, I mean five or six times. So our premium is pretty big. It's big versus anybody. It's healthy versus anybody. Our pricing, we have pricing power, but we're at the top already. So it would be wrong to think that the 7.3% growth in our business had much of a pricing component to it, 30 basis points, 40 basis points that's it. So we don't really price.

When I hear our people talk about competitors, they never – actually, they never talk about competitors. They talk about how we're doing versus ourselves, because Snap-on is a unique product. Remember, I'm not a lifer, so none of what I say is really due to me, but people either decide to buy Snap-on, or decide among a bunch of others. It's pretty much it in any product line. You ask any mechanic that – if you ask a mechanic, like I said, 70% say Snap-on, 8% is number two, diagnostics that's for hand tools, 63% – these are independent surveys, 63% to 8% in diagnostics; 47% to 11% in power tools; 63% to 13% in tool storage, if Nick Saban had these scores, he would be happy.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

A couple of questions I put together here as it relates to the van productivity and the stronger growth that you've seen, the organic growth you've seen in the traditional hand tools business. Can you talk how much of that is about the productivity initiatives and – I am going to draw a couple of things together...

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Yeah.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

You've got productivity initiatives, how much of it is increased use of credit in the marketplace? And how much of it is the competition in just the competitive environment, either you playing catch up or you getting ahead of the competitive landscape?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

I would never comment on the competitors. I think there are formidable companies in the van business, MAC and Matco. Stanley is a very strong company and capable, but MAC is a small piece of the large, large empire. Matco is a company inside of Danaher, who has moved its tool – has moved its factories out of the corporations, so that may be a factor, but let's now talk about them.

I think the big factor for us is productivity improvement. We've looked at optimizing and breaking through the traditional barriers to the van, the time of the van driver. This is a scarce resource, less than 30% of time spent selling. That's why they only call 850,000 technicians when there are 1.3 million. Our productivity activities have helped them to do more.

And then space, we've implemented marketing activities in terms of Rock 'N Roll vans and TechKnow vans that have time shared space and amplified the space of the van. That has helped us. On top of this, we've become better at new product, our new product. We've learned how to better utilize that intelligence from the market, from the workplace and brought it into product development. And if you think about it, a company that produces a complex array of products, 65,000 SKUs, is asymmetrically enabled by modern technology like 3D printing and finite element of analysis. And so we've been able to bring out...we measure new product by hit products, million dollar sellers in the first year. Last year, we had four or five times, the number we had in 2006. And that all these three things have accrued to help our Tools Group.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Yeah, great. Question here on the Ford new F-series pick-up truck, aluminum body on that. Does that have any potential opportunity for you in terms of selling equipment and from a shop owners' perspective, body shop who need to work on it, do they need new equipment? Any idea on that?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Well, the body shops will need new equipment for sure…

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Is that an opportunity for you?

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

That's some opportunity for us, although not so big a piece of our revenue is collision. It's mostly big in Europe, so to the extent they're big in Europe that will help us. There are a lot more fasteners on the F-150 and that should help our business in terms of selling hand tools. I mean the hand tool business, everybody thinks the hand tool business is maybe kind of a Silas Marner type business. And I ask you this, we sell hand tools, we guarantee them for life. The number of technicians aren't growing. Why is that we have any business in hand tools at all? And the reason is like the F-150, they keep changing. And so they need more hand tools. In fact, against all odds, since the rise of the electronics, 50 engine codes on a car in 1995, thousands today, hand tool demand has only gotten bigger. And so this is a kind of thing because the cars keep changing and people keep packing in more geometries and creating different geometries that people need different hand tools. The average technician has now bought 16 different ratchets and they need more, I can assure you and we're ready to sell them different versions.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Time for one last question, anything from the audience? Then let me close the loop here, then on the last piece of your business, we didn't really touch on Snap-on Credit.

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Yes.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

How does that fit into the business model? What surprise…

<<Nicholas T. Pinchuk, Chairman, President & Chief Executive Officer>>

Snap-on Credit is really a credit company. It's a strategic arm of the Tools Group. It's focused on supporting big ticket sales. Fundamentally, it's a great business model. You've got to take a look at it, because it's a business model that has a yield about 16% to 17% and has all in life-cycle losses of 3%, great profitability and its volume follows the expansion of the Tools Group. One thing we learned, it used to be a 50:50 joint venture. Now it's 100% owned joint venture and the simpatico that occurs from being a 100%, not a joint venture, 100% owned company, has driven Tools. In other words, the financing activities are more in line with what will generate more tools sales and that's exactly what's happened, its one of the reasons why Tools has grown.

<<David Leiker, Analyst, Robert W. Baird & Co., Inc. (Broker)>>

Wonderful. Thank you. With that, management will be available for a breakout in the Oak Room on the 7th floor. Please join me in thanking Nick for his time.