

SNAP-ON INCORPORATED

Moderator: Leslie H. Kratcoski
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9:00 am CT

Operator: Good day and welcome to the Snap-on Incorporated 2017 First Quarter Results conference call. Today's conference is being recorded. At this time, I'd like to turn the conference over to Leslie Kratcoski. Please go ahead.

Leslie Kratcoski: Thanks, Lauren and good morning, everyone. Thanks for joining us today to review Snap-on's first 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 have 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, Snap-on.com, under Investor Information. These slides will be archived on our website along with a 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.

Finally, 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 earnings release issued today, which can be found on our website.

With that said, I'd now like to turn the call over to Nick Pinchuk: Nick?

Nick Pinchuk: Thanks, Leslie. Good morning, everybody. As usual, I'll start the call by covering the highlights of our first quarter. Along the way we'll look at results, the markets, the progress we've made and I'll give you a perspective on what we believe it all means. Then Aldo will move into a more detailed review of the financials.

We believe that our first quarter is convincing confirmation of Snap-on's ability to continue its trajectory of positive results, to overcome period to period variations from business to business, to offset macroeconomic headwinds and to still keep advancing along our runways for both growth and improvement.

Our reported sales in the quarter of \$887.1 million were up 6.3% including \$29.1 million in acquisition related sales partially offset by \$9.6 million in unfavorable foreign exchange.

Organic sales, organic sales growth was 4.1% with increases registered by every group. Those gains, together with continued contributions from Snap-on value creation processes, the principles we use every day, safety, quality, customer connection, innovation and rapid continuous improvement, or RCI, combined to author another encouraging quarter.

Our EPS was \$2.39, up 10.6% from last year's \$2.16. The increase includes an OpCo operating margin of 19.1%, 50 basis points higher than last year, and that rise overcame a 50-basis point unfavorable impact from acquisitions. When you combine those current OpCo gains with earnings of \$52.5 million from Financial Services, it brings Snap-on's consolidated operating margin to 23%, up from the 22.5% in 2016.

Now let me pause here to note that these acquisitions may be margin attenuators at this point, but they're actually landscapes that are fertile ground for Snap-on value creation. As we go forward they're actually great opportunities to achieve margin improvement, margin growth.

Now let's look at the market. We believe the auto repair market remains relatively robust. The Tools Group, organic sales growth, somewhat lower than in previous quarters, but still positive, solving technician problems and making our franchise network more prosperous and more powerful.

And in the Repair Systems and Information, or RS&I Group, another vehicle repair business, encouraging strength in the quarter, expanding Snap-on's presence in the garage, capitalizing on a broader product line. With innovative new tools like the Digital Thermal Imager and new acquisitions like Car-O-Liner, all leading to growth in independent repair shops as well as OEM dealerships across the group.

C&I, the businesses that serve critical industries, a wide range of industries, and is the most international of our groups. And in the quarter, the results showed progress despite some challenged industrial sectors and some troubled geographies. In critical industries, improvement in the natural resources segment, overcoming the continuing economic turbulence in places like the Middle East and the impact on our international aviation business.

At SNA Europe, mid-single digit growth with strength in places like the UK, Spain, France, Italy, in the Nordic region, mitigating difficulties in Eastern Europe. And from our Asia Pacific division, solid increases in key countries like China and India. So overall, I describe our C&I markets as improving. Challenges still exist, but we took advantage of the opportunities that were available and we're encouraged by our advancements in the quarter.

And those activities together with our auto repair related businesses, combined to drive overall progress along our runways for growth, enhancing the van network, expanding with repair shop owners and managers, extending to critical industries, building in emerging markets.

Advancements leveraging our widening product line and increasing our understanding of work, growth in critical sectors and important geographies. That's an overview of the markets.

Now let's talk about the segments. In the C&I Group, organic sales were up 3% with mid-single digit growth in the European Hand Tools business and low single digit rise in volume to our customers in critical industries. From an earnings perspective, C&I operating income was \$41.6 million representing an operating margin of 13.9%, a decrease of 40 basis points which reflects higher investment spending for product development and engineering activities in that group.

As part of C&I, we remain committed to extending in critical industries and we'll keep strengthening our position to capture new business opportunities in those areas as they arise.

Along those lines, we've seen some recent gains with natural resources customers helped by our lineup of innovative new products designed especially to make work easier in that uniquely challenging industrial setting. Oil and gas can be tough. We have the products.

One example is our collection of Snap-on 3/8" drive torque adapters, manufactured in our Elizabethton, Tennessee plant. It's a new product family used in applications where access is difficult and precision is critical, in natural resources, in mining, on a variety of large earth moving equipment.

Produced from special high alloy steel, precision forged and then specially heat treated, these tools have a double hex 12-point design that allows fasteners to be engaged every 30 degrees instead of the standard every 60 degrees, a feature that provides better angles for grip and easier operation in restricted areas. The adapter length, crucial for measuring torque, is very precise and it's etched on the tool for easy reference. The new torque adapter family is a great addition to our lineup and it fills a vital need for our critical industry customers.

Now I already mentioned SNA Europe's mid-single digit organic sales growth. That progress was broad based across the landscape including some, what I would say, were fairly difficult regions and countries. SNA Europe's positive trend to performance now extends 14 straight quarters with year over year sales growth. And that string includes 16 straight quarters of margin improvement. It's quite a record in a region that's marked by so much uncertainty.

Now onto the Tools Group, organic sales up 2.5%. The operating margin was 17.2%, the operating margin of 17.2% was up 60 basis points versus the 16.6% recorded last year. And that's despite 70 basis points of unfavorable foreign currency. Let me say that again, 17.2%, up 60 basis points against 70 basis points of unfavorable currency.

The Tools volume story simply put, our TechKnow vans kept humming. Our TechKnow vans kept humming, but the Rock N Roll Cabs were less effective, and that big ticket combination was less favorable than usual. We do believe, however, that this runway for coherent growth enhancing the franchise channel, remains very strong. And there's evidence of that strength of an ongoing positive trajectory across the van channel, in our franchise metrics, the important financial and physical indicators that we monitor, we monitor them very closely, and again this quarter they remain favorable.

There's also testimony in our direct interactions with the franchisees at events like this year's kickoff meetings, held all over the network. At the very recent meetings with the national

franchisee advisory council, and at separate interactions with individual franchisees, all of these have been marked by enthusiasm and optimism.

Our franchisees, all of them, entrepreneurs and professionals are confident in reaching higher and optimistic regarding the upcoming opportunities. And some of that enthusiasm rests on the new product that's rolling out to drive new excitement. For example, a great addition to our tool lineup is the Snap-on FLLF 80 3/8" drive ratchet. Again, manufactured in Elizabethton, Tennessee.

Comes with a flexible head, extra-long handle, better access in tight automotive applications and additional leverage within those - that's what the long handle's for - additional leverage within those cramped spaces. It's got a sealed head to keep lubricants in and contaminants out and that bodes a longer life. And of course it includes the Snap-on's patented - our patented dual 80 technology featuring 80 teeth - 80 teeth gear for minimum swing arc and dual pawls for strength. You put these 80 teeth together, small swing in the arc, dual pawls make it strong. You've got the long handle for leverage, a design for flexibility, strength and compact operation. We believe we've got a great hand tool in our new 3/8" extra-long flex head ratchet. And you've heard me talk about hit products before, it will be one of this year's hit products. We're also rolling out a new tool storage program, a brand new color, striking trim options, some great new promotions. We all know that tool storage activity thrives on excitement, well our new package is aimed at creating that buzz and based on early reactions, it'll do the job.

Also just recently launched was the Snap-on PT850 half-inch drive impact wrench. It's a signature product. A top of the line pneumatic offering that has the power of our MG725 but providing a more enhanced balance for comfort and control and durability. Comfort in a lighter weight package, better grip positioning for improved balance with ergonomic improvements to reduce fatigue when you're using it all day.

Control, a compact design with a featherable trigger for applying the right torque for the job, easy to control, even while wearing gloves in the shop. And durability, two-piece housing with an aircraft grade aluminum nose, solid steel impact mechanism, forged steel frame and hammers, and a precision cast hard-coated aluminum cylinder. Going to last a long time. Made in our Murphy, North Carolina facility, the new Snap-on PT850 half-inch drive impact is a great wrench. Power, comfort, control and durability. These are the features our customers want in a power tool and early sales confirm that this tool is right on target.

Now let's speak of RS&I. First quarter organic sales rose 7.8% with high single digit gains registered pretty much across the board – with diagnostics and information product, independent shops, with the businesses focused on OEM dealers and with undercar equipment. And on a reported basis, including the group's - the RS&I Group's \$21.3 million of acquisition related sales, first quarter volume rose 14.3% compared to last year.

Operating earnings of \$78.7 million increased \$9.7 million from 2016 and operating margin of 24.7% was flat with last year, but with strong volume and RCI improvement offsetting 140 basis points of negative impact from the acquisitions. Remember what I said before, fertile ground for margin improvement.

We're clearly seeing the potential of our runways for growth in the RS&I Group, expanding Snap-on's presence in the garage with coherent acquisitions providing greater reach, like in collision repair in Car-O-Liner's and new - really new capabilities and products for our team and they can wield them.

RS&I's organic growth in the quarter was broad. It was broad based across every division. Now I just mentioned the progress with independent shop owners, and those gains were clearly evident in the ongoing success of our powerful MODIS Edge handheld and the spread of the digital thermal imager. It's becoming an essential product for top-flight mechanics.

The rise can also, you know, that rise, that gain can also be seen in our latest software release, which not only contains expanded new model coverage, but also incorporates additions like motorcycle information and enhanced key fob reprogramming. It's sold quite well and it's fortified our advantage in - our clear advantage in comprehensive repair, vehicle repair information.

For undercar equipment, sales were up high single-digits. Contributing to that increase was RS&I's introduction of the smart speed tire changer, the new unit - this new unit incorporates Snap-on's proprietary and patented technology to minimize floor to floor or tact time needed to mount a tire. A big factor in shops was handling a lot of tires, and there and are quite a few of those high-volume locations. You can see them everywhere.

Tires are more sophisticated and more difficult to change than ever. Low profile tires for example, make up 25% of the market and are growing and their rigid construction makes them more susceptible to handling damage and require much more - they require much more care during the tire changing process. Our smart speed systems eliminate a great deal of that risk. It continuously monitors the power to the motor and automatically selects the turntable speed at which the motor has the correct amount of torque to mount the tire without harm and in the fastest time.

We often speak of customer connection activities and observation in the workplace, gaining insights to make work easier for our customers. Well, repair shop owners and managers are continually seeking the highest possible throughput. We observed that tire damage by torque mismatch is a big contributor to delay in those shops. So for owners and managers, the smart speed tire changer that matches that torque to the tire, makes life easier and saves time and saves money. It's a great addition to the equipment line and initial customer feedback has been quite enthusiastic, really enthusiastic.

Finally, RS&I got a real boost in the quarter by the increased activity from OEM dealerships, up high single-digits, driven in particular by several significant essential diagnostic and essential tool programs for large automotive, heavy duty trucks and agricultural OEMs. It appears as though the focus on repair across the industry continues to be robust.

So those are the highlights of the quarter, overcoming headwinds, continued progress, organic sales rising 4.1%, gains achieved through our Snap-on Value Creation Processes, strengthening our businesses and driving to its 19.1% OpCo operating margin, up 50 basis points, overcoming the acquisition, and EPS of \$2.39, up 10.6%. It was an encouraging quarter.

Now let's turn the call over to Aldo. Aldo?

Aldo Pagliari: Thanks, Nick. Our consolidated operating results are summarized on Slide 6. Net sales of \$887.1 million in the quarter increased \$52.9 million or 6.3% from 2016 levels, reflecting a \$33.4 million or 4.1% organic sales gain, \$29.1 million of acquisition related sales, and \$9.6 million of unfavorable foreign currency translation.

Foreign currency movements adversely impacted our Q1 sales comparisons by 130 basis points. The organic sales gain reflects continued progress in serving the vehicle repair sector as well as further recovery in sales to Industrial market segments in our C&I Group. Consolidated gross margin of 50.5% improved 70 basis points, primarily due to the benefits from higher sales and savings from RCI initiatives.

Operating expenses of \$278.5 million yielded an operating expense margin of 31.4% in the quarter, an increase of 20 basis points as operating expenses for acquisitions and unfavorable foreign currency effects were partially offset by benefits from sales volume leverage.

As a result of these factors, operating earnings before Financial Services of \$169.5 million, increased 9.1% and as a percentage of sales, improved 50 basis points to 19.1%. The operating margin of 19.1% in the quarter reflects a 50 basis point impact from acquisitions and 20 basis points of unfavorable foreign currency effects.

Financial Services revenue of \$76.8 million increased \$10.5 million from 2016 levels, and operating earnings of \$52.5 million, including \$0.3 million of unfavorable foreign currency effects increased \$5.5 million.

Consolidated operating earnings of \$222 million, including \$4.1 million of unfavorable foreign currency effects increased 9.7%, and the operating margin of 23% improved 50 basis points from 22.5% a year ago.

Our first quarter effective income tax rate of 30.7% compared to 31% last year.

Finally, net earnings of \$141.6 million, or \$2.39 per diluted share increased \$13.3 million, or 23 cents per share from 2016 levels, representing a 10.6% increase in diluted earnings per share.

Now let's turn to our segment results. Starting with C&I Group on Slide 7. Sales of \$298.7 million in the quarter, increased \$11.7 million, or 4.1%, reflecting an \$8.6 million, or 3% organic sales gain, \$7.8 million of acquisition-related sales, and \$4.7 million of unfavorable foreign currency translation. The \$8.6 million organic sales increase primarily includes a mid-single-digit gain in the segment's European-based hand tools business, and a low single-digit increase in sales to customers in critical industries, with improving sales trends in the natural resources segment.

Gross profit in the C&I Group of \$116.6 million compared to \$110.5 million last year. The gross margin of 39% improved 50 basis points, primarily due to favorable foreign currency effects partially offset by a 10 basis point impact from acquisitions.

Operating expenses of \$75 million in the quarter compared to \$69.4 million last year. The operating expense margin of 25.1% increased 90 basis points primarily due to increased cost including, higher cost for research and engineering activities, and 20 basis points of operating expenses for acquisitions.

As a result of these factors, operating earnings for the C&I segment of \$41.6 million, including \$0.9 million of favorable foreign currency effects, increased \$0.5 million from 2016 levels. The operating margin of 13.9% decreased 40 basis points from 14.3% last year.

Turning now to Slide 8. First quarter sales in the Snap-on Tools Group of \$409.4 million increased \$6.9 million, or 1.7%, reflecting a \$10.1 million, or 2.5% organic sales gain and \$3.2 million of unfavorable foreign currency translation. The \$10.1 million organic sales increase reflects higher sales in both the U.S. and international franchise operations.

Gross profit of \$177.1 million in the quarter compared to \$173.2 million last year. Gross margin of 43.3% improved 30 basis points, primarily due to the benefits from higher sales and savings from RCI initiatives, partially offset by 60 basis points of unfavorable foreign currency effects.

Operating expenses of \$106.8 million in the quarter were essentially flat for 2016 levels. The operating expense margin of 26.1% improved 30 basis points primarily due to sales volume leverage.

As a result of these factors, operating earnings for the Snap-on Tools Group of \$70.3 million, including \$3.7 million of unfavorable foreign currency effects, increased \$3.6 million. And the operating margin of 17.2% improved 60 basis points.

Turning to the RS&I Group, shown on Slide 9. First quarter sales of \$318.8 million increased \$40 million, or 14.3%, reflecting a \$21.6 million, or 7.8%, organic sales gain, \$21.3 million of acquisition related sales, and \$2.9 million of unfavorable foreign currency translation. The 7.8% organic sales increase was broad based, primarily reflecting high single-digit gains in both sales of undercar equipment and sales of diagnostic and repair information products to independent repair shop owners and managers, as well as a high single-digit increase in sales to OEM dealerships.

Gross profit of \$154.3 million in the quarter compared to \$131.6 million last year. And the gross margin of 48.4% improved 120 basis points, primarily due to the benefits from higher sales and savings from RCI initiatives, and 70 basis points of benefit from acquisitions.

Operating expenses of \$75.6 million in the quarter compared to \$62.6 million last year. The operating expense margin of 23.7% increased 120 basis points principally due to 200 basis points of unfavorable impact from acquisitions, partially offset by benefits from sales volume leverage.

Operating earnings for the RS&I Group of \$78.7 million, including \$1.0 million of unfavorable foreign currency affects, increased \$9.7 million from prior year levels. The operating margin of 24.7% was unchanged from last year, despite 140 basis points of impact from acquisitions.

Now, turning to Slide 10. Operating earnings from Financial Services of \$52.5 million on revenue of \$76.8 million compared to operating earnings of \$47 million on revenue of \$66.3 million last year. Financial Services expenses of \$24.3 million increased \$5 million, primarily due to changes in both the size of the portfolio and in the provisions for credit losses.

As a percentage of the average portfolio, Financial Services expenses of 1.3% in the quarter compared to 1.2% last year. The average yield on finance receivables of 18.0% in the quarter was up slightly from 17.9% last year, and the average yield on contract receivables of 9.3%

compared to 9.5% last year. Originations were \$264.6 million in both the first quarters of 2017 and 2016.

Moving to slide 11. Our quarter-end balance sheet includes approximately \$1.86 billion of gross financing receivables, including \$1.63 billion from our U.S. operations. Approximately 82% of our U.S. financing portfolio relates to extended credit loans to technicians. In the first quarter, our worldwide financial services portfolio grew \$48.7 million, or 2.7%. As for finance portfolio losses and delinquency trends, these are tracking somewhat higher year-over-year, but continue to be in line with our expectations in view of an appropriate risk reward balance in this segment part of our business. Additionally, the 60-day delinquency rate in the U.S. extend the credit portfolio improved by 20 basis points in line with typical seasonality. Overall, profitability in the Financial Services segment rose by 11.7% in the quarter, primarily as a result of our year-over-year growth in the portfolio.

Now turning to Slide 12. Cash provided by operations of \$192.4 million in the quarter, increased \$50.8 million from comparable 2016 levels, primarily due to higher 2017 net earnings, \$14.9 million of proceeds related to the settlement of a treasury lock, and changes in other operating activities, including \$5 million of lower discretionary contributions to our U.S. pension plans year-over-year.

Net cash used by investing activities of \$81.7 million included additions to finance receivables of \$227 million, partially offset by collections of \$173.8 million. Capital expenditures of \$18.6 million in the quarter compared to \$19.5 million last year.

During the first quarter, we also acquired BTC Global Limited for \$9.2 million. Based in the United Kingdom, BTC designs and implements automotive vehicle inspection and management software for OEM franchise repair shops and is included in the Repair Systems & Information Group.

Net cash used by financing activities of \$66.6 million included the January 2017 repayment of \$150 million of notes at maturity and a \$135.7 million net decrease in other short-term borrowings. In the quarter, the company also received \$297.8 million of net proceeds from the February issuance of \$300 million of 3.25% unsecured long-term notes. The proceeds of which were used to repay commercial paper borrowings, with the remainder to be used for general corporate purposes.

Dividend payments to shareholders totaled \$41.2 million in the quarter, and the company repurchased 210,000 shares of its common stock \$35.8 million under its previously announced share repurchase programs.

Turning to Slide 13. Trade and other accounts receivable increased \$9.3 million from 2016 year-end levels, largely due to \$8.4 million of foreign currency translation. Days sales outstanding of 63 days was unchanged from year-end. Inventories increased \$26.3 million from 2016 year-end, primarily to support continued higher customer demand and new product introductions. Foreign currency translation contributed \$8.5 million of the increase. On a trailing 12-month basis, inventory turns of 3.3X were unchanged from 2016 year-end levels.

Our quarter-end cash position of \$123 million, increase \$45.4 million from 2016 year-end levels. Our net debt to capital ratio of 24.7% compared with 26.3% to 2016 year-end. In addition to \$123 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 access to the commercial paper markets. As of quarter-end, we had no commercial paper borrowings outstanding.

That concludes my remarks on our first quarter performance. I'll now turn the call back to Nick for his closing thoughts. Nick?

Nick Pinchuk: Thanks, Aldo. Well, that's our first quarter. C&I with organic growth of 3%, OI margin 13.9%. SNA Europe, continuing its bellwether trend, sales up, profits up, again. Industrial, critical industries coming back with broader gains. Tools up 2.5% organically, OI margin of 17.2%, up 60 basis points against the currency headwind of 70 basis points. RS&I organic sales up 7.8% with increases across each of its customer bases. OI margin of 24.7% flat versus last year, but with RCI and volume offsetting 140 basis points of acquisition impact. It all added up to an overall organic growth of 4.1% and OpCo OI margin of 19.1%, up 50 basis points against 50 basis points of impact from acquisitions. And an overall EPS of \$2.39, up 10.6%.

It was an encouraging quarter, achieved against headwinds and variation. And we believe, as we've said for some number of quarters, that we're well positioned to continue that trend. Great new products are entering the mix, aimed at customer needs and customer excitement, all drivers of progress along our runways for growth. And Snap-on Value Creation continues to drive us down our runways for improvement. And now, we have the new landscape of our acquisitions providing expanded possibilities for further margin improvement.

We believe we have abundant opportunity for both growth and improvement. And we believe we possess the capabilities and the intent to take full advantage and continue our positive trend going forward to 2017 and beyond.

Before I turn the call over to the operator, I'm going to - I'd like to speak to our franchisees and associates. I know many of you are listening. The encouraging quarter we're announcing today reflects your unique skill and commitment. For all your many contributions to our progress, you have my congratulations. And for all your extraordinary dedication to our team, 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. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star 1 to ask a question. We'll take our first question from Christopher Glynn from Oppenheimer.

Christopher Glynn: Thanks good morning.

Nick Pinchuk: Good morning.

Christopher Glynn: Yes, just with the Tools Group, you've had some deceleration recently, but the comparisons were pretty tough in the first quarter and start to get a little easier. So, you know, right now, you're a little bit below what I think you'd call normalized. Is there a reversion that, based on the comparisons that you expect?

Nick Pinchuk: Well, look. We always say that we expect the 4% to 6% growth for our divisions and there could be variations from quarter-to-quarter. You know, we never necessarily predict a reversion based on comparisons. This particular one was a difficult comparison like you said. I think the better thought is, look, we feel pretty confident about the new products we're rolling out. We're kind of pumped about the whole idea of the long handle ratchet and the new tool storage program and color and the excitement that will generate and the idea of the PT850 half inch impact, which is a signature tool, and everybody loves it. We like those. And so at the end of the day, it comes down to product, and we're kind of optimistic about that, that's what I'll say.

Christopher Glynn: Okay, and then any update on franchisees, inventories and sell through against contracted sales to franchisees?

Aldo Pagliari: No, I'd say the - we're in line with franchisee movements more or less. There's always some variation in their inventory levels, but pretty much in line and reflective of our sales.

Nick Pinchuk: Yes, and that moves from time to time. You know, that goes, quarter-to-quarter the franchisees' sales won't particularly match ours. It really depends on how they're feeling and the programs and so on.

Christopher Glynn: Okay. And then with the originations and sort of a flattening trend, but portfolio continues to grow, can you talk about any trend of restructuring or re-aging the loans and how you view that?

Aldo Pagliari: We don't restructure the loans. I mean, the loans stand by themselves and the originations, I think, largely reflect the pattern of what's being demanded in that channel and as Nick has mentioned earlier, tool storage, which is the most popular product to be originated on the contract was not as robust a quarter in that regard.

Christopher Glynn: Okay, great. And then just, do you have any data on the net charge-offs and the ending allowance?

Aldo Pagliari: Yes, they were up slightly if you look at it year-over-year, but stable and actually on a sequential basis, we saw a bit of improvement over all. So again, somewhat stable trends in line with our expectations.

Nick Pinchuk: Yes.

Christopher Glynn: Okay thanks guys.

Aldo Pagliari: Sure.

Operator: Our next question comes from David MacGregor with Longbow Research.

David MacGregor: Yes, good morning everyone.

Nick Pinchuk: Good morning.

David MacGregor: Yes. Good morning, Nick. A lot of good things this quarter. I wanted to just - I wanted to ask you about the storage and I'm just trying to get a sense of what's going on there with your assessment of the negative growth in storage. Is this demand easing? Is it maybe curtailed credit availability with respect to this category?

(Crosstalk)

Nick Pinchuk: No, I don't think it's any of that. Sorry, I don't think actually, I don't think it's any of that. I mean, there always can be factors, from time to time. My assessment is first of all, you know, tool storage has been growing a long time. This quarter even though it was down is one of our top 10 quarters ever still in tool storage. But having said that, you know, now we've had two quarters of tool storage, you know, less than robust positioning, and we conclude, maybe it needs a little more excitement, maybe, you know, at the end of the day, these are product-driven. You know, and you roll out a product and some - some of them are singles and doubles and some are home runs. And when we look at tool storage in general, you might be tempted to say that when we look at the tool storage offering across the network, it's down in four of the five places where we have vans. And they aren't affected by any of those things that you're talking about, you know, in other words, if you observe those markets over the years, they wouldn't be affected by, let's say, credit or so much by credit or by saturation. And so we conclude the tool storage line up just need a little goosing. So that's why I'm talking about this new program rolling out with new colors and so on. It's as simple as that, I think.

David MacGregor: Has there been any change in the number of Rock 'n Roll Cab Expresses on the road?

Nick Pinchuk: No, we haven't changed them. So that's another thought. You know, I mean - but we - I tend to think it's for our - it's - this tends to be - there is a lot of factors, David. You know, and of course, everything I say isn't true everywhere. You know? But the thing is, I think if you look across the networking and you see the behavior of tool storage and when it happens for two - for more than one quarter, it starts to get your attention. We say, "Hey, let's accelerate a little goosing." And that's what we're doing.

And so I think that's what we've concluded in the tool storage situation. You know, it's not big ticket because diagnostics is rolling. Diagnostics is having a great quarter, had a great quarter, another great quarter. So that isn't it. It isn't the big ticket situation, just - and you see it from time to time. It doesn't show up so clearly, but when we look at it at a granular level, we see positives and, you know, singles and doubles and triples.

David MacGregor: I want to ask you about the acquisitions because as you highlight you've got a lot of margin upside there. I guess I was going to ask you if you could just quantify your best guess on what the margin upside is? Do these acquisitions get back to kind of fleet average margins? Or could they surpass that? What's the upside?

Nick Pinchuk: Well, you know, I don't really want to speculate on that. You know, all I know is we ought to be moving them upwards. You know, you've got a year where they come in. You know, you kind of have a year where they start to - their comparing to the year before where they weren't in the number, but then after that, given Snap-on Value Creation and so on, you expect to have that effect, start moving them upwards.

And I don't know where the upside is I mean you got Car-O-Liner there which is a kind of equipment level business, which is at the bottom of RS&I's, you know, OI margin. Remember, RS&I has a variance of several thousand basis points in its OI margins and equipment is at the sort of bottom end of that because it's hardware-based. And Car-O-Liner starts out a little bit lower than that. We think we got a lot of upside in those businesses. And so - but I wouldn't want to quantify it. I am just happy to get a good chunk every year.

David MacGregor: Did I hear you correctly?

(Crosstalk)

Nick Pinchuk: No limits to the upside.

David MacGregor: right, did I hear you correctly that it takes about a year to integrate but after a year you - they should not be...

(Crosstalk)

Nick Pinchuk: I don't mean integrate. I don't mean integrate. I just mean that's the arithmetic, you know.

In other words, if you have a lower margin business and you're comparing to the year, the year before, you don't have it in your numbers in the year before. So it stands out like a sore thumb, you know, it's a variance. And then when you - so you don't - it might be less impactful the next quarter even if it gets better and less impactful, but it's still going to be dilutive for a couple of quarters. But then, you start to have comparisons where it's in the base, and you see your improvements stand out vividly, see what I mean.

David MacGregor: Yes, absolutely. You got a very good free cash flow story, do acquisitions become a more predominant part of the growth as we go forward from here?

Nick Pinchuk: Well, I think we've always said that we're going to acquire along our runways for growth, and we have a, you know, sort of a list of acquisitions we're reviewing constantly. I think acquisitions - I wouldn't necessarily think they're going to become more a greater part of the growth, but we're constantly reviewing them and you can see us take advantage when the opportunities are there.

David MacGregor: Last question is just how do you promote growth of a second associate on the truck? On those trucks where you do have a second associate, it seems like they're getting superior growth to those that don't have it. How do you incent your franchisees...?

(Crosstalk)

Nick Pinchuk: Well, I think it's stuff like - it's, you know, we do two things, one is we try to make sure that there's a sharing of best practices at colloquial meetings like the kickoffs, like the NFAC. The NFAC people are representatives, and they'll go back and share it with their regions. And then of course, at the SFC, the Snap-on Franchisee Conference where pretty much all of them come, we try to make sure we trumpet the effect of those things and talk about and provide seminars on how to select and manage those people. And also, on our own, we try to provide packages that will support them. They're not our employees, and we don't urge these - it's a situation. It's important to say, "This is not our program." But we provide the support programs that make it possible.

David MacGregor: Got it. Thanks, Nick.

(Crosstalk)

Nick Pinchuk: Thank you.

Operator: Our next question comes from Liam Burke with Wunderlich.

Liam Burke: Yes good morning Nick. Good morning Aldo.

Nick Pinchuk: Good morning, Liam.

Aldo Pagliari: Good morning.

Liam Burke: Nick you've put a lot of upfront investment in emerging markets in the C&I business. You highlighted the fact that in the - India and China are doing well. Are you starting to see any kind of positive operating return off those upfront investments?

Nick Pinchuk: Well, they're profitable, but we keep investing, you know. So I mean, the thing is, the balance is still about where it's always been, so we don't necessarily see - I don't see a time where we're going to see huge upside coming there because we still see opportunities in terms of top end, so we keep trying to reposition ourselves in terms of Blue Point stores, for example. We added another one this quarter as part of the C&I expense category.

And so I don't think we're seeing a boost out of them in terms of the financials yet. This is just our view that they're going to give us returns, and our approach is still, Liam, that we want to build the physicals, because we have confidence that as that, you know, that wave comes and it starts to come, it starts to come, you know, we're going to see returns. But, you know, we don't view it as a huge profit opportunity in the near-term, more or less as a positioning opportunity.

Liam Burke: Good, thanks, Nick. And Aldo, on the cash flows, just touching, returning there. Even when I'm adjusting for some of the one times, your cash flow growth is starting to accelerate. Beyond acquisitions, where is the priority for cash allocation going to be?

Aldo Pagliari: Well, the first priority still always remains serving our organic growth. So we're not afraid to make investments. We talked a little bit about that in the C&I segment. But when there's opportunities to invest internally, we're willing to do that as well. And of course, Snap-on Credit still is growing. That's been a user of our cash to some extent, and then as Nick mentioned already, support of acquisitions.

Liam Burke: Okay. Thank you, Nick. Thank you, Aldo.

Nick Pinchuk: Sure.

Operator: Our next question comes from Scott Stember with C.L. King & Associates.

Scott Stember: Good morning, guys.

Nick Pinchuk: Good morning.

Scott Stember: Can you maybe talk about some of the new programs or the new tools and products you talked about in the Tools Group? Really, just talking about the new tools, the new, you know, cabinet program, new colors. Is there anything else to this new program outside of color? And maybe just talk about the timing of when these new products will start showing up in your numbers.

Nick Pinchuk: Well, we're talking about sort of the beginning of, you know, sort of like as we go forward into the second quarter and, you know, you're talking about trim as well as programs that wrap around it, so you have kind of programs that try to make sure that people focus on this as well. And so those things are what wraps around the kind of thing.

It has to do with, one an attraction that gives someone a reason to buy. This is what we say in the Tools Group. You know, there are - they're ongoing types of programs, a lot of programs that roll through this, but we're talking about it's aimed at the Tools Group, aimed at a new product that's going to get peoples' attention. And we wrap merchandising program around this and promotion program around this and maybe throw in, you know, some sort of hat or something like that, that gets people. So you give people a reason to pay attention to it. And we think when they pay attention to it, they see those colors with that trim, with the features that are available, this becomes a seller. And, you know, the Algona plant has, I think, you know, an incredible amount of different options that can be add on to this kind of thing.

So we feel pretty good about it. It's a new - like I said, it's a new set of - it's a new appearance that people won't have seen before, and we think that drives excitement. One of the things that it does, if you're in a garage and a guy's got a box, you like the appearance of a different box, you like some of the features of a different box. He wants trade out because he wants to get attention in his orb. This is what generates the activity.

Scott Stember: Got it. And then the RS&I side, you're starting to see some continued, you know, growth here in the - with the new car, the OEM dealers. Can you maybe just talk about what you're seeing there? Are these sustainable trends? And, you know, the high single-digit growth that we're seeing in this segment, if this is something that can persist, you know, throughout the year?

Nick Pinchuk: You know, I don't know. Look, I think these are program-related. So that particular segment of the business with OEM dealerships tends to be more lumpy than others, you know, because you get a program and sometimes, that program lasts for three quarters and it runs out and you don't hook onto another program till you get out to the fifth quarter. So there's a gap quarter in there. That's - if you listen to these calls enough, you'll hear me talk about that stuff.

But what I am encouraged about this time is, we have vehicle OEMs, we have heavy-duty OEM's, we have heavy-duty OEMs, we have agriculture OEMs doing this. So it's a kind of broad view of repair. We haven't seen that so much come together. So it's kind of positive in that regard. Now I can't testify that these are going to continue, because as I said, this tends to be a lumpy portion of our business. But the fact that it's spread across three different places, pretty good.

Scott Stember: All right, and last question on currency, you know, Brexit happened, I believe, in the end of the second quarter last year. Is it still a good assumption that in the back half of the year, we should expect the currency comparison to ease?

Nick Pinchuk: Yes, although the second quarter, we think, you know, look, we state today, if the currency stays the way it is today, the second quarter will be somewhat tougher from a currency point of view because the, you know, other currencies were stronger in the second quarter, then they deteriorated. But you're right in terms of - it gets - the comparisons get easier as it flows out. So what we would, you know, again, it will probably - the chances of it staying right where it is today is probably low, but if did, we'd see some rise in currency difficulty going forward to the second quarter and then abatement in the third and fourth quarter.

Scott Stember: Got it, that's all I have. Thanks for taking my questions.

Operator: We'll go next to Tom Hayes with Northcoast Research.

Tom Hayes: Hi thanks, good morning gentlemen.

Nick Pinchuk: Good morning.

Tom Hayes: Just wondering, Nick, if we could dig into the C&I segment just a little bit. You know, last year, we were talking about, you know, three of the end markets: energy, military and avionics

certainly a bit of challenge in 2016. Just want to see kind of what your thoughts are coming out of Q1 and for the balance of the year for those three segments?

Nick Pinchuk: Actually, you know, I'm pretty encouraged. You know, C&I is a big place, you know, for us. We got SNA Europe, which I just - if you're going to talk about C&I, SNA Europe is a bellwether. You know, that thing has become a monster. It's growing 14 quarters in sales and 16 quarters in profits. And Europe, I don't know if you've noticed lately, isn't the most certain of places, so it's done pretty well. But if you want to go to critical industries, like I think you're referring to, which is about 1/3 of the business in C&I, you know, we did focus on military and natural resources and aviation. And natural resources came back for us.

And, you know, what I like about this quarter is, it is about the same growth in the critical industries as past quarters. Although sequentially, it looks pretty positive, but also, it's a little bit more broadly based. Last quarter, we had growth, but there were more eggs in the military basket, the military got better by wider - by a pretty wide margin last quarter, and that delivered the critical industry's basket for us.

This time, we have gains in natural resources in places like wind and mining and places like that, and oil and gas, and gains in heavy-duty and gains in general industry, a little more broadly based. Military is more tepid. In fact, it's down a little bit this quarter, difficult to predict where military has gone from quarter-to-quarter. I said that for a dog's age on these calls.

And then aviation still isn't solved because for us, the Middle East, you know, the international aviation business is kind of on its back because a lot of that business came out of the Middle East and it isn't working for us right now. So you're going to see some kind of recovery outside. You got military, which is chronically variable, and the rest of them are kind of recovering. Aviation, we still haven't quite solved yet.

Tom Hayes: Okay great.

Nick Pinchuk: So think positive, positive. I'm really encouraged.

Tom Hayes: Okay. And then Aldo, you start on the financial services piece, I think you kind of covered it a little bit. I just want to make sure I understood the components. You saw the EBIT margin go down year-over-year from about 70.9 to 68.4. I think you called out, I think it was manpower and additional write-offs. Was that kind of the driver of the change there?

Aldo Pagliari: You're talking about financial services?

Tom Hayes: Yes.

Aldo Pagliari: Yes. No, financial services there's certainly higher provisions for receivables over the last couple of quarters. We had that phenomenon in Q4. All I'm saying is that if you look year-over-year your provisioning is higher, albeit a little bit less than what we had done in Q4 and you're seeing a little bit of progress on the 60 plus day delinquency indicator.

Tom Hayes: Did you also mention, I thought you mentioned in your prepared remarks you - did you add manpower to the financial services business?

Aldo Pagliari: Yes. Little bit of additional...

(Crosstalk)

Tom Hayes: Okay. All right, thank you.

Operator: Our next question comes from David Leiker with Baird.

Joe Vruwink: This is Joe Vruwink for David.

Nick Pinchuk: Yes, Joe

Joe Vruwink: Can you maybe comment on growth trends in the tools channel as the quarter progressed?

And I'd be interested in whether these tax refund delays maybe impacted February at all and you started to see activity come back in March as refunds came back?

Nick Pinchuk: No, I don't think so. I don't - we didn't see the tax refund delays. We didn't hear anything like that. You know, generally, the week-by-week or month-by-month trends in our quarters don't really mean much. We have quite a bit of variation, you know, it's sort of like quarter-to-quarter - quarterly variation in the month. So it really doesn't mean so much.

What I will tell you though is that I met just - we had - we boxcared this quarter. In the beginning, like middle of January, we met with the franchisees and they were booming. And then at the end of the quarter, a couple of weeks ago, I met with the franchise - the National Franchisee Council for the US. They were really enthusiastic.

So at least from the windshield surveys, I felt pretty good about it. The numbers are what they are. I still think, you know, the growth was, you know, it was fairly positive for a retail business. But again, we had, you know, and we had - so we don't think it's the market. The market is very positive for us, we think.

Joe Vruwink: So when I look at your loan origination growth and let's say that's flat, therefore big ticket sales are flattish, to do 3% organic growth in Tools implies the core hand tool category, which is obviously the majority of what you're selling, is maybe mid-single-digit growth directionally.

Nick Pinchuk: Look, first of all, let's talk about, you know, let's talk a little bit about big ticket. Big ticket, you got diagnostics up. What drives the originations is big ticket. But there's a new kind of wrinkle in this, and that is the thermal imager in diagnostics. This is, you know, a smaller-end diagnostic, you know, in effect like in the \$1000 range. And what had been in diagnostics almost uniformly being financed by the credit companies is being - some of that is being financed by the franchisees, because now they are strong enough to finance something like that. So that's part of what's going on in the originations activity.

You know, and there are other categories besides hand tools, there's power tools, there's some other stuff, which we call shop and tech and so on. So I don't think you can make just that view of the world. You can - you could kind of step back and make it. But you can't just look at originations in this case and say that big ticket is completely flat, because you have that thermal imager in there this time, which makes it different.

Joe Vruwink: So I guess - yes, so this is what I'm trying to get at. The industry, it seems to be growing at a mid-single digit pace. When you listen to your peers talk about their growth, seems to be mid-single. And when I look at Snap-on and consider that a lot of the products that have seen strong growth this cycle that are tied to originations, those have flattened out.

If I look at the other stuff in the Snap-on portfolio, it would seem to be growing mid-single, so at the end of the day Snap-on still growing in line with its market. It's just we're weathering these comparisons right now where you have a particular big ticket category you called out tool storage, that is just going through a bit of a soft patch.

Nick Pinchuk: Yes, there's some of that. That's directionally probably correct. You know, I think our big message here today is, we think the market is pretty good.

Joe Vruwink: Yes. Okay, great. Thank you, guys.

Nick Pinchuk: Sure.

Operator: Our next question comes from Bret Jordan with Jefferies.

Bret Jordan: Good morning, guys.

Nick Pinchuk: Good morning.

Bret Jordan: Hey. On the corporate expense, the 21 and change, that's, you know, pretty well-controlled.

I think a year or two ago, you talked about it sort of being \$100 million annual run rate. Should we think about that being more along the lines of 20? Or was that \$5 million lower pension contribution the driver to the low number?

Nick Pinchuk: Okay. Look, I think, Bret, the way I would say it is, I think we spent something - let me think. I think we spent about \$94 million last year in the corporate expense. I think you could say it's going to be in that ballpark, maybe uplifting it slightly. That's the kind of number I would expect. These things ebb and flow back and forth from quarter-to-quarter, so I would model it in that range, if I were you.

Bret Jordan: So the \$5 million lower pension contribution was sort of just a timing issue around the first quarter.

Aldo Pagliari: No. Just to clarify. It's Aldo. The pension contribution doesn't really impact expense directly in the short run. Pension is relatively flat year-over-year. That's just the contribution that goes into the pension plan. So that's not a direct cause and effect. So if you look at corporate expenses, they're kind of flattish really the last year in Q1. Pension is up so slightly over year-over-year. So

I'd say, you're trending directionally to be, as Nick said, \$95 million to \$100 million range is still for modeling purposes, not unreasonable.

Bret Jordan: Okay. And then a question, I guess - I'm sure the franchisees are communicating with their customers daily. Is tool storage, is that - I mean, obviously, it's more of a discretionary transaction versus diagnostics where you need the current technology to complete the job. Is there an issue there that this is sort of an indicator of mechanic sentiment? Or is it just that there's nothing new enough and the channels just spur them to buy again.

Nick Pinchuk: Look, I think it's always the case. You know, you can bring out a new power tool or a new diagnostic threat and it can be, let's say, double as my - my baseball analogy instead of a home run. I'm not saying that our offering is tremendously, you know, better. It's - we think it's strong, but it may not be as compelling as it was the last iteration. It may not be the home run. That's a difference.

I do think you're right in that tool storage is a little more emotional. You know, you look at that box, you say, you know, I remember being on an event once. A guy came at a fair, where this guy said, hey, did you see that white box with a sapphire trim? I really love it. I think I've got to buy it. He was so excited by just the appearance of the box. So that is the fact in this kind of thing. It's not a saturation thing.

Bret Jordan: Okay. What's the color that's coming out?

Nick Pinchuk: I don't know if I'm allowed to reveal that, actually, you know, Bret...

Bret Jordan: I mean, I'm going to wait to buy my Snap-on box if I see the new color of that.

Nick Pinchuk: Yes, you're right, right.

Bret Jordan: On average yield and it's up 10 basis points, I mean, I think it was a year ago this quarter we talked about some of the platinum franchisees allowed to be more flexible I think in their decision, their credit decisions. Is yield up because we've got - we've change the borrowing base a little bit? Or is that yield just up because we have seen some interest rate increase year-over-year?

Aldo Pagliari: Look, I think it's more reflective of the actual credit profile, what we're doing the underwriting on. And as I said, it's actually down 20 basis points from last quarter. So 18%, 17.9% is kind of the natural range that settles in that, so there really hasn't been a lot of movements on yields of over the recent turn.

Bret Jordan: Okay. All right, great. Thank you.

Nick Pinchuk: Thank you.

Operator: We'll go next to Robert - or excuse me, Richard Hilgert with Morningstar.

Richard Hilgert: Thanks for taking my questions. Good morning, everybody.

(Crosstalk)

Richard Hilgert: Just curious, you know, with the administration talking about tax reduction. You know, I've noticed your tax - effective tax rate consistently runs, you know, about 5 percentage points below the corporate average. If we were to see a reduction from the corporate rate of 35%, down to a 25% number, would your effective tax rate move the same amount or - are there anything - any things in your taxes that would change that ratio? Would it be less of a change? More of a change?

Aldo Pagliari: Well, first off, Richard, when you look at the overall rate of 31%, you have to remember, we're about 80% influenced by the United States, 20% influenced by - let's say the outside world's tax rates. So you're right. If you go back to the 35% statutory federal rate Snap-on takes advantage of probably around 250, a little bit more, slightly more than that of deductions, such as the manufacturing deduction, the R&D tax credit, things of that nature.

So if you took a step back and look strictly at US taxes as written today, you'd say, well, we're in the 33% range, maybe the 32.5% range. So in theory, if a statutory rate is reduced from 35% to something less than 30%, Snap-on should actually stand to benefit on the US effective tax rate. As you know though, these are pretty complicated items being discussed, so you see the actual rollout of the tax law, it's really hard to opine on what the impact will be.

Richard Hilgert: Understood. Just for clarification, on the C&I group, Nick, you were saying military was a slight headwind, aviation was a headwind, but natural resources were positive. The European region was positive, doing very well. Is that the correct summary?

Nick Pinchuk: That's correct.

Richard Hilgert: Okay, great. And then I was curious, you know, with the way that the growth rates have been going in RS&I, you know, and you were mentioning some of the dynamics of the big ticket items, could you maybe describe, you know, the growth rates there, more in terms of, you know, what's been your experience with respect to the overall pricing in that group versus the overall volume in that group? And how much does each one affect the growth rate.

Nick Pinchuk: Wow, you know, I don't know. I mean, the thing is, look, all I can say is, we haven't - we don't have pricing generally as one of our line items in explanation. We don't see much motion in pricing. And so generally, when we - and at both ways, when we price, we tend to do it around

the new model which resets the value proposition and therefore the prices get reset. We don't like to reduce our prices, you know, to get volume, and so we resist that.

Richard Hilgert: Right.

Nick Pinchuk: And we do so in equipment. And so from time to time, it can happen. But in general, you are not seeing us knock down the prices. And if you doubt that, remember what I said, 24.7% OI margin against 140 basis points negative year-over-year impact from acquisitions, that means something good had to happen that was worth of 140 basis points.

Richard Hilgert: Right.

(Crosstalk)

Richard Hilgert: Right. And you mentioned one item that you thought would be on the hit parade this year in the hand tools group. Given, you know, the kind of tapering off there, the last couple of quarters, you know, your - what you said about your hit parade in years past is that you've got, you know, \$1 million per year coming in from the hit parade from the new items that are going out.

Has that kind of tapered off in the last couple of quarters and then we can expect to see more of that kind of come back a little bit above that? Or how has that all playing out right now?

(Crosstalk)

Nick Pinchuk: I don't know. What we actually measure, Richard, is the number of million-dollar products, not the amount. So you can have Transformers, and you can have, you know, some other small - you can have the Jack Reachers, both of which make some money but aren't necessarily a lot -

are quite different in terms of the amount of money they'll have. Transformers is a huge blockbuster, Jack Reacher made some money so, you know, so that kind of thing.

And so that what's happening in these things. You know, maybe a few the hit products didn't make us much, maybe a few of tool storage that's came out didn't sell quite a much, and they still were hit products.

What I'm talking about in this particular one is, is that, that's going to be hit product. We say it's going to sell a lot more than that particular one will sell a lot more than \$1 million. Our numbers of hit products though have continued to be pretty good, so they're not really abating. It's just the amounts that are being associated with it.

And hit products aren't the whole thing, it is that the hit products that drive everything. Hit products drive the excitement so there's a whole bunch of non-hit products that are driving excitement some of which are former hit products that are older. So it's a more complex - the revenue add-up is a more complex thing. I don't think you can look at a trend in the big new success - difference really.

Operator: Thank you. That concludes today's question-and-answer session. At this time I'd like to turn the conference back to Leslie. Please go ahead.

Leslie Kratoski: Thanks, Lauren. We appreciate everyone for joining today. A replay of the call will be available shortly on snaon.com. And as always, we appreciate your interest in the company.
Thanks.

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

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