Operator: Please standby. Good day, and welcome to the Snap-on Incorporated 2016 Third Quarter Results Conference Call. Today’s conference is being recorded. At this time, I would like to turn the conference over to Leslie Kratcoski, Vice President of Investor Relations. Please go ahead, Ma’am.

Leslie Kratcoski: Thanks, Rachael, and good morning, everyone. Thanks for joining us today to review Snap-on’s third 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 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, 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 the 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 Q3 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, everyone. As usual, I’ll start with the third quarter highlights, provide an update on the environment and speak about some of our trends. Aldo will then provide a more detailed review of the financials.

In the third quarter, we again showed progress along our runways for growth – along our runways for growth and for improvement. And we saw those gains across all our operating segments. Total reported sales were $834.1 million, up 1.5%, and that included $9.7 million of unfavorable currency. It also included the incremental $1.1 million of sales from last year’s acquisition of Ecotechnics. Organic sales were up 2.6% and the OpCo operating margin, it was up 140 basis points, reaching 18.9%. When you add in the $50.6 million of operating earnings from Financial Services, and that was up from $43.5 million in 2015, the consolidated operating margin was 23%, an increase of 180 basis points. Our EPS was $2.22, up $0.24, a double-digit increase, rising 12.1% from last year.

Let’s consider the environment. Let’s look at that environment. Automotive repair continues to be favorable. And we believe our Tools Group and our Repair Systems and Information, or RS&I group, they’re both well-positioned to take full advantage of that opportunity. The Tools Group clearly demonstrated enhancements to the franchise network, gains in both the North American and European markets, continuing to make the most of the opportunities so abundant in an aging and changing vehicle fleet.
At RS&I, serving repair shop owners and managers, sales progress was mixed. The volume of diagnostics and repair information products to independent shops was up mid-single digits. For the OEM side, activity with individual dealers was up while programs commissioned by the OEM manufacturers, a historically lumpy space, was down. Undercar equipment was flat with variations from product line to product line.

For Commercial and Industrial, or C&I, the group was up organically 1.5%. Snap-on Europe – SNA Europe was higher again, making progress against the turbulence of Brexit and the other uncertainties across its market. The Industrial business was flat, reflecting the challenges, you know, we’ve seen now for a year. Significantly, however, the critical industry activity recorded its second straight quarter of sequential growth following more than a year of decreases, reductions driven by the difficult microenvironment in areas like oil and gas, military, and the Middle East.

Now, there will always be headwinds across our operations. They’ve been a factor in other quarters and they were present in the third quarter, but we did overcome. We did keep growing because we’re well-positioned to confront the challenges and continue to proceed down our runways for growth, enhancing the franchise network, expanding with repair shop owners and managers, extending to critical industries and building in emerging markets. These do represent our growth strategies and we continue to make progress along those corridors.

At the same time, those growth drivers are joined and supported by the benefits of Snap-on Value Creation – safety, quality, customer connection, innovation, rapid continuous improvement or as we call it, RCI. Together, these are the processes, the tools we use each and every day to drive improvement. And improvement is written all over our results, especially customer connection, understanding the work of professional technicians and innovation, matching that insight with technology to make work easier.
Snap-on Value Creation once again led to more prestigious awards. We were recently honored with two MOTOR Magazine Top 20 and with five Professional Tool & Equipment News, or PTEN Innovational Awards. But, you know, those winners represent only a fraction of a wide array of new products born out of the insight of our franchisees and our direct salespeople, translating workplace observations into productivity solutions. And in the quarter, those customer connections were a big factor in our results. To see some of that, let’s move to the individual groups.

Commercial and Industrial, organic sales up with an operating margin reaching 15.1%, an increase of 80 basis points from the last year’s 14.3%. The benefits of Snap-on Value Creation evident in the ongoing stream of innovative new products developed for the critical industries. One of those products launched in the third quarter by our industrial division is the PWZ5 Pliers Wrench. This wrench is the latest and the largest model in our popular Snap-on PWZ series. It’s long, 41.75 inches. It can handle jobs that would traditionally require a pipe wrench, but with much less slippage, for better overall performance and for better safety. It features inwardly angled teeth, fine at the back, large at the front for a stronger and more secure grip on objects of all sizes. And the narrow jaw design gives improved accessibility in tight compartments and in those cramped corners. It’s perfect for applications on tie rods and other areas that are hard to reach, in industries like railroad, oil and gas, and for servicing fleets – actually, any heavy-duty application. You heard me speak about – in the past about our growing industrial product line. Well, this wrench is another great addition to our hand tool lineup for critical industries.

Now, SNA Europe. Twelve quarters in a row of year-over-year growth, navigating some difficult geographies and some tepid economies. SNA Europe sales activity continues to be positive, but its profits are even more encouraging, now up for 14 straight quarters, and we believe there’s still more opportunity. And the Asia Pacific operations, mixed environments across the regions. We continue to invest in building our physicals, and the Asia operation had gains, contributing to the progress in the quarter.
So that's C&I, now on to the Tools Group. Organic sales, up 5.6%, significant growth both in the U.S. and internationally. Operating income of $64.6 million compared to $56.3 million in 2015. The operating income margin of 16.3% rose 150 basis points from last year's 14.8%. Volume gains as well as operating improvements from RCI translated into a significant margin rise. And that 150-basis point gain, it overcame 60 basis points of negative currency.

When you consider the Tools Group success, you can see the power of Snap-on Value Creation, of customer connection and innovation. The MOTOR Top 20 and the PTEN awards represent just a few examples of the recognitions our products continue to receive. You know, awards from industry publications, but also awards from the professionals that use our tools every day. Innovation has consistently been a key contributor to our Tools Group and, in the third quarter, more new products. Like our reversible ratcheting combination wrench, the latest in the lineup of Snap-on wrenches, adding a reversible feature to our patented ratcheting mechanism. Utilizing our Dual 80 technology, combining dual pawls with thin walls, box-end design, smooth operation, more torque transference in tight spaces and, of course, it incorporates the iconic Snap-on flank drive profile, biting into fasteners without rounding corners, preventing slippage. The new reversible ratcheting combo wrench, it's more turning power, enhanced durability, compact design and built stronger to last longer.

This is the core of Snap-on Value Creation, customer connection and innovation, solving specific problems in the shop. Take the new 20 millimeter 12-point impact socket. Born from hours of observations in the workplace – hours of observation in the workplace, this socket is designed to remove head bolts in large industrial engines, long enough to reach the deepest of inset bolts and strong enough to remove the toughest fasteners, a unique combination. It’s produced in our Elkmont, Alabama plant, and it's essential for servicing large off-road equipment. It may not be needed often, but when it is, it’s critical and Snap-on has it. It's just another example of our commitment to make work easier, solving our technicians’ most challenging problems.
The third quarter is also when we hold the annual Snap-on Franchisee Conference, our SFC. This year, it was in Orlando, with more than 8,700 attendees, franchisees and family members from over 3,000 routes. Three days of showcasing the opportunities to enhance the franchise channel. And I can report to you because I was there, that based on the optimism and the confidence of our franchisees, it was a big success. And orders – because we take orders at these events – and orders, well, they were up once again, beating the record levels of 2015.

And when we speak of the van channel, we also have to consider the strategic contributions of Snap-on Credit. Our financial services arm helps create opportunities across the organization, but especially within the Tools Group. It’s been an ongoing partnership for over 50 years. And our credit company had a strong presence at this year’s SFC, supporting franchisees with unique programs. You know, 270,000 of our approximately 875,000, about 30% of our technician customers in the United States have credit company contracts, enabling sales of those big ticket items. The credit company’s been a key part of the franchisees’ success and the third quarter was no exception to that.

Now, let’s move to RS&I. Organic sales were up 1.7%. The operating margin up 25.1%, it increased 50 basis points from the 24.6% registered last year. As I mentioned, RS&I clearly showed progress in providing repair information and diagnostics to independent shop owners and managers. And certainly, a portion of that growth came from innovative new products, several launched at the SFC, products like the MODIS Edge, our latest diagnostic offering, an enhanced industrial design, improved ergonomics, reduced weight and code scan capability that allows the tech to scan all of a vehicle’s computer systems with the push of a single button. It also contains fast access oil change and reset information, automatic vehicle identification and our unique SureTrack expert database, all features specifically designed to save the technicians significant time. This new handheld is lighter, faster and smarter, and simply based on the excited crowd of franchisees at the SFC that carved out precious time to attend MODIS Edge hands-on training, we expect it to be a very popular item.
Another exciting SFC launch was our Diagnostic Thermal Imager. This completely new Snap-on offering is a breakthrough in pinpointing problems, with a graphical display illustrating surface temperature data, and a reference library of nominal and out-of-spec thermal images for a variety of auto parts found in brakes, emission systems and in vehicle electrical equipment. We believe we have a winner with the Diagnostic Thermal Imager and orders at the SFC prove it. It sold out.

And RS&I innovation wasn’t just in diagnostic products. Take the brand new Polartek air conditioning unit, from our recent acquisition, Ecotechnics, developed and manufactured specifically for the North American market, meeting a very aggressive launch. Both our U.S. and our Canadian customers have affirmed the strength of the unit’s design and performance. It’s been a real testament to the capability of the Ecotechnics team.

And speaking of products, of getting more to sell to repair shop owners and managers, this week we entered into a definitive agreement to acquire Car-O-Liner, based in Gothenburg, Sweden, but reaching around the globe. Car-O Liner’s product offering and its special expertise are important additions to the Snap-on team, providing extraordinary capabilities in collision repair, a segment where change is now authoring opportunity. It’s an operation that strengthens our position both in auto and in heavy-duty. Car-O-Liner is another coherent business and we believe that matched with the Snap-on team, it offers substantial possibilities for both growth and for improvement. All of that great opportunity going forward.

So that’s the highlights of our quarter. Organic sales up 2.6%, gains across all groups, progress along our runways for growth. Snap-on Value Creation, turning our customer connection insights into innovative new products, and along with our ongoing RCI initiatives, driving margin improvement. And it all shows in the results. OpCo OI margin rising to 18.9%, up 140 basis points, EPS of $2.22, up 12.1%. It was an encouraging quarter.

Now I’ll turn the call over to Aldo. Aldo?
Aldo Pagliari: Thanks, Nick. Our third quarter consolidated operating results are summarized on slide 6. Net sales of $834.1 million were up $12.6 million or 1.5%. Due to the strengthening of the U.S. dollar, foreign currency movements adversely impacted our Q3 sales comparisons by 120 basis points. Excluding $9.7 million of unfavorable foreign currency translation and $1.1 million of acquisition-related sales, organic sales increased 2.6%, reflecting continued progress in serving the vehicle repair sector as well improvements in sales in our Commercial and Industrial segment.

Consolidated gross margin of 50.2% improved 70 basis points from 2015 levels, primarily due to benefits from higher sales and savings from RCI initiatives. Operating expenses of $261.5 million yielded an operating expense margin of 31.3% in the quarter, an improvement of 70 basis points, primarily due to sales volume leverage and lower pension expense. As a result of these factors, operating earnings before financial services of $157.6 million, including $4 million of unfavorable foreign currency effects, increased 9.7% and, as a percentage of sales, improved 140 basis points to 18.9%.

Financial services revenue of $71.6 million in the quarter increased 17.2% from 2015 levels. And operating earnings of $50.6 million increased 16.3%. Consolidated operating earnings of $208.2 million, including $4.5 million of unfavorable foreign currency effects, increased 11.3%, and the operating margin of 23% improved 180 basis points from 21.2% a year ago.

Our third quarter effective income tax rate of 31.2% compared to 31.6% last year. For the full year, we now anticipate that our 2016 effective income tax rate will be slightly below our full year 2015 rate of 31.7%.
Finally, net earnings of $131.7 million, or $2.22 per diluted share, increased $14.9 million, or $0.24 per share, from 2015 levels, representing a 12.1% increase in diluted earnings per share.

Now let’s turn to our segment results.

Starting with the Commercial and Industrial, or C&I Group, on slide 7, sales of $289.3 million in the third quarter increased modestly over 2015 levels. Excluding $3.5 million of unfavorable foreign currency translation, organic sales increased 1.5% primarily due to a mid single-digit increase in the segment’s European-based hand tools business, and a low single-digit increase in both the segment’s power tools and Asia Pacific operations. Organic sales to customers in critical industries were essentially flat as a decline in the aerospace market segment was largely offset by a gain in sales to the military and increases in both the technical education and natural resources market segments. Despite the continued presence of certain headwinds in the industrial space, we were encouraged that sales performance has improved from what we had seen earlier in the year.

Gross profit in the C&I Group of $112.7 million compared to $109.5 million last year. The gross margin of 39% improved 110 basis points primarily due to savings from RCI initiatives and 40 basis points of favorable foreign currency effects. Operating expenses of $69 million in the quarter compared to $68.2 million last year. The operating expense margin of 23.9% increased 30 basis points, primarily as a result of higher costs, including costs associated with continued expansion initiatives in Asia, and 10 basis points of unfavorable foreign currency effects. As a result of these factors, operating earnings for the C&I segment of $43.7 million, including $0.3 million of favorable foreign currency effects, increased $2.4 million from 2015 levels, and the operating margin of 15.1% improved 80 basis points from 14.3% last year, representing a recent high for C&I, and up 130 basis points sequentially.

Turning now to slide 8. Third quarter sales in the Snap-on Tools Group of $397.2 million increased 4.4%. Excluding $4.6 million of unfavorable foreign currency translation, organic sales
increased $21.2 million or 5.6%, reflecting mid single-digit gains in both the company’s U.S. and international franchise operations. Gross profit of $173.3 million compared to $166.5 million last year. Gross margin of 43.6% declined 20 basis points as benefits from higher sales and savings from RCI initiatives were more than offset by 60 basis points of unfavorable foreign currency effects. Operating expenses of $108.7 million in the quarter compared to $110.2 million last year. The operating expense margin of 27.3% improved 170 basis points primarily due to sales volume leverage and savings from RCI and other cost reduction initiatives. As a result of these factors, operating earnings for the Snap-on Tools Group of $64.6 million, including $3.2 million of unfavorable foreign currency effects, increased $8.3 million and the operating margin of 16.3% improved 150 basis points from 14.8% last year.

Turning to the Repair Systems & Information, or RS&I Group, showed on slide 9. Third quarter sales of $286.1 million increased 1.1% from 2015 levels. Excluding $2.8 million of unfavorable foreign currency translation and $1.1 million of acquisition-related sales, organic sales increased 1.7%. The organic sales increase primarily reflects a mid single-digit gain in sales of diagnostic and repair information products to independent repair shop owners and managers. In the quarter, sales of both undercar equipment and sales to OEM dealerships were essentially flat. As Nick mentioned, sales to OEM dealerships this quarter were particularly impacted by the timing of essential tool and facilitation program sales. For example, sales in Q3 of last year benefited from a refrigeration-related facility action program which has since lapsed.

Gross profit of $133.1 million compared to $130.9 million last year. And a gross margin of 46.5% improved 20 basis points primarily due to savings from RCI initiatives, partially offset by 10 basis points of unfavorable foreign currency effects. Operating expenses of $61.3 million in the quarter compared to $61.2 million last year. The operating expense margin of 21.4% improved 30 basis points principally due to savings from RCI initiatives. Third quarter operating earnings for the RS&I Group of $71.8 million, including $1.1 million of unfavorable foreign currency effects,
increased $2.1 million from prior year levels. And the operating margin of 25.1% improved 50 basis points from 24.6% last year.

As we announced earlier this week and as Nick mentioned in his remarks, we have entered into a definitive agreement to purchase Car-O-Liner. Car-O-Liner's annual sales were approximately $95 million and we expect them to generate operating income margins somewhat similar to those of RS&I's undercar equipment business, which are typically in the low teens. We expect to complete the acquisition of Car-O-Liner within the next month. Our plan is to fund the transaction with a combination of cash on-hand and approximately $125 million in issuances of commercial paper.

Now, turning to slide 10. Operating earnings from Financial Services of $50.6 million and revenue of $71.6 million compared to operating earnings of $43.5 million and revenue of $61.1 million last year. Financial services expenses in the quarter included some additional headcount related expenses to help better serve our growing portfolio, but as a percentage of the average portfolio, financial services expenses were 1.2% in both periods. The average yield on finance receivables of 18% in the quarter compared to 17.9% last year. And the average yield on contract receivables of 9.4% compared to 9.5% last year. Originations of $269.8 million in the quarter increased 4.7% from prior year levels.

Moving to slide 11, our quarter-end balance sheet includes approximately $1.8 billion of gross financing receivables, including $1.6 billion from our U.S. operation. Approximately 81% of our U.S. financing portfolio relates to extended credit loans to technicians. In the first nine months of 2016, our worldwide financial services portfolio grew $190.3 million. As for finance portfolio losses and delinquency trends, these continue to be in line with our expectations.

Now, turning to slide 12. Cash provided by operations of $111.9 million in the quarter decreased $1.8 million from comparable 2015 levels, as higher net earnings were more than offset by $11.4
million of higher cash tax payments and $5.4 million of higher U.S. pension contributions. Net cash used by investing activities of $69.2 million included $56 million to fund a net increase in finance receivables and $16.5 million of capital expenditures.

Turning to slide 13, trade and other accounts receivable increased $26.6 million from 2015 year-end levels reflecting both higher sales and an increase in days sales outstanding, from 60 days at year-end to 63 days at third quarter end. Inventories increased $25.8 million from 2015 year-end levels, primarily to support continued higher customer demand and new product introductions. On a trailing 12-month basis, inventory turns of 3.3 compared with 3.5 turns in 2015 year-end.

Our quarter end cash position of $117.5 million increased $24.7 million from 2015 year-end levels. The net increase includes $501.7 million of cash collections from finance receivables and $415.6 million of cash from operations. These cash increases were largely offset by the funding of $691.4 million of new finance receivables, dividend payments of $106.3 million, the repurchase of 492,000 shares for $76.4 million, and $56.6 million for capital expenditures.

Our net debt-to-capital ratio of 22.6% compared with 24.6% at 2015 year-end. In addition to our $117 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 third quarter end, we had $8 million of commercial paper borrowings outstanding.

That concludes my remarks on the third quarter performance and I'll now turn the call back over to Nick.

Nick Pinchuk: Thanks, Aldo. Stepping back and looking at the Snap-on third quarter, we believe a number of things are apparent. Our part of the auto repair market is solid. As we’ve seen in the past, it follows a different trajectory than new car sales. It was reliable even in the withering
recession of 2009 and it’s strong today. And we believe our ability to take advantage of that opportunity grows every quarter, and you can see it in the results.

Tools Group, sales up 5.6% organically. The franchisees, more prosperous and stronger. The group’s OI margin, up 150 basis points against 60 basis points of unfavorable currency. The credit company continues to serve as the Tools Group’s strategic partner, enabling franchisees and technicians as it has done for five decades through recession after recession without disruption.

RS&I, selling to repair shop owners and managers, mixed growth, encountering the usual ups and downs of OEM-sponsored programs, but showing real progress with individual shops, both independents and dealers.

And C&I, amidst turbulence, but now growing again, showing, year-over-year, in sequential gains, despite the difficult macros. And despite the difficult macros, registering an operating margin of 15.1% up 80 basis points, showing what we believe is confirmation of the great value it offers as a runway for coherent growth.

And finally, in the results, you can see the effects of Snap-on Value Creation, more new products driving gains, and the engine of rapid continuous improvement authoring efficiency. It all came together for organic sales growth at 2.6%, and an OpCo operating margin of 18.9%, up 140 basis points. And an EPS of $2.22, an increase of 12.1%, a double digit gain again.

And the Car-O-Liner acquisition, giving us more to sell, more opportunities for coherent growth and providing more possibilities for the Snap-on Value Creation to drive progress. It’s a great opportunity. It was an encouraging quarter, and we believe it clearly confirms the future of continuous Snap-on growth and improvement as we move to the end of this year and into 2017 and beyond.
Before I turn the call over to the operator for questions, I'll speak directly to our franchisees and associates. I know many of you are listening or will listen to this call. Once again, you should know that the encouraging performance of our corporation is only possible because of your capability, your energy, and your dedication. For your extraordinary contributions to our progress, you have my congratulations, and for your unfailing commitment to our team, you have my thanks.

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

Operator: Thank you. At this time, if you would like to ask a question, please press * then the number 1 on your telephone keypad. If you’re using a speaker phone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, that’s * then the number 1 to ask a question.

We’ll take our first question from David Leiker with Baird.

Joe Vruwink: Hi, good morning. This is Joe Vruwink for David.

Nick Pinchuk: Hi, Joe – hello, Joe.

Joe Vruwink: I wanted to discuss the deceleration in origination growth this quarter. So maybe for context, can you revisit the driver of the double digit origination growth that’s been seen in recent quarters, and then maybe comment on whether demand conditions or other items changed for those same drivers or those same products in the current quarter?

Nick Pinchuk: Sure, look. A couple of things, first of all, big ticket – you know, the idea of Snap-on tool storage – tool storage and diagnostics was – were strong in the quarter, in fact, stronger than – so much stronger than the overall Snap-on Tools growth, and incidentally, just as a side, hand
tools were also pretty strong in the quarter. So it’s still a good quarter for big ticket items, which are the principal drivers for these things. Secondly – and the reason that is the case, the reason why big ticket has been the case is because we’ve been investing, in product – great new tool storage products, and a number of the features and a number of great attractive products that get customers excited. The fact that diagnostics are more important in the repair shop than ever before, and technicians and – are trying to, you know, I guess, caliber up, to have better and bigger diagnostics to take care of those products. It’s natural that big ticket items would be stronger, so you would see that.

So I think that, looking at the Tools Group and seeing that lead the way is just a consequence of our investment in the marketplace with the kinds of products we’ve had, and the demands of the market associated with – the shift in the market associated with more diagnostics, and also, our investment and enabling events that break through the original, structural barriers of the – of the vans, that is, the space and time, the Rock N’ Roll Cabs, which we’ve talked about quite a bit, which helps Tool Storage and the TechKnow vans – you know, we have 67 of them now, and the TechKnow vans, we have 49 of them, and that drives fairly robust, bigger ticket item sales.

In terms of, you know, higher double digits before – you know, double digit originations before and the somewhat less originations now, you can’t trace quarter-to-quarter because there isn’t a perfect one-for-one correlation. Remember that, when you’re looking at originations, you’re looking at franchisee sales. When you’re looking at the Tools group, you’re looking at our sales. So we sell to the franchisees, so the timing is different. Then you have on top of that, the franchisee’s margin, and then on – you have on top of that, the idea that a tool storage sale or a diagnostic sale may ignite a couple of trade-in type sales, which would also be somewhat supported by EC – by the – by the credit company. So you put those altogether, and that shows the landscape, but when we step back and we look at the, say, 2015 numbers, when we look at the 2015 numbers about origination and the tools group big ticket sales, they seem pretty much the same. And this year, we’re starting to see year-to-date, the same kind of thing.
Joe Vruwink: So I’m sure you know, in the market, there seems to be this idea that Tools Group growth is only strong because origination growth is strong. This quarter, you actually maintained the strong rate of growth – organic growth, stable quarter-over-quarter, originations came down. That either, to me, seems like the hand tool category may be strengthened quarter-over-quarter, or this whole relationship of painting Tools Group as a byproduct of the credit business maybe isn’t the most accurate relationship.

Nick Pinchuk: Well, it isn’t the most accurate. The Tools Group is a strategic partner – I mean; the credit company is a strategic partner of the Tools Group. But if you think about it, yeah, okay, but only 270,000 of our 875,000 customers have an – have a credit company contract. That’s only about 30%. So if you think that – you know, if you think that the Tools Group growth is being driven exclusively by the credit company mojo, I think, think again because it just isn’t that wide. Of course. It has grown because the market has the – you know, the customers have turned that way and we have invested in to support that with new product, and also, part of the way we figured out how to enable the van has been associated with that – with that segment, but it’s a natural thing. I’ve been talking about the Rock N’ Roll Cabs for multiple quarters, and that would naturally, of course, drive a little bit more credit company activity. Okay?

Joe Vruwink: And then my last question, if I can. You know, the comps were difficult, so to do the growth you did this quarter was positive. I’m just thinking, you took 3,000 routes down inter-quarter for the franchisee conference. Is there any indication, based on just vans coming back online and your order activity that the pace of sales is going to strengthen year-over-year in the Q4?

Nick Pinchuk: You know, I’m not in the business of projecting out. You know, I’ll only say this, what I said on the call. Look, the franchisee conference was boffo. It was really good. And the enthusiasm was good, so I can tell you anecdotally – and anybody who was there will tell you
anecdotally, I was just with the national franchisees – the National Franchisee Advisory Board and they’re all positive. And a quantitative piece is, the orders were up significant – you know, it was up over the record that we set last year at the SFC. Now, they don’t translate one to one in sales. They were up significantly. It doesn’t translate one to one, but what it says is, our guys saw the new products. They were confident in the future, they invested in it and they ordered, so they think good things are coming.

Joe Vruwink: Great. Thank you.

Nick Pinchuk: Sure.

Operator: We’ll take our next question from Liam Burke with Wunderlich.

Liam Burke: Thank you. Good morning, Nick. Good morning, Aldo.

Nick Pinchuk: Liam, how you doing?

Liam Burke: Aldo, on your prepared statement, and I guess Nick, you can answer, you talked about the physicals and the investment in emerging markets in C&I. Are you seeing any kind of significant revenue growth there to begin absorbing that upfront investment?

Aldo Pagliari: Well, emerging markets tend to have their own volatility and lumpiness, so to speak, for lack of a better word, but we believe that the secret to penetrating the emerging markets is to establish physical presence, people, place, products that suit those markets and those environments. So through thick and thin, you know, we’re continuously looking for opportunities to expand our footprint because we know that what we have today could still be improved upon. So that’s basically our philosophy when it comes to that, Liam.
Nick Pinchuk: Yeah, we’re investing in things like more blue-point stores, more products, you know, you try to expand your product line, and more sales outlets. For example, we just opened another sales outlet in Vietnam this quarter. So that’s the kind of investment we’re doing, because in the 11 years I lived in Asia, I know, I’m confident that the building of the physicals allows you to take advantage of the market as it – as it matures.

Liam Burke: And the same with C&I, on the new product introductions, you talked about that being a big driver of incremental growth. Are there any particular verticals that you – this quarter, saw opportunity to put the new product into the market?

Nick Pinchuk: Well, we had – we talked about a couple of those. You know, in this particular market, the natural resources, we’ve been – you know, I can only say that, actually, we’re trying to play the long game in this end. We believe we’re trying to build our activity in each of these markets. So for example, not in this particular quarter, because we wouldn’t make products that’s [inaudible] quarter. We see opportunities, we build out – our goal is to build up in each of the markets. For example, last year, we brought out 920 new products just for aviation, 313 for oil and gas, even though it was, you know, having probably one of the most difficult times, 313 for the military, even though it was difficult times. So we just keep adding, not so much targeting. Now, we saw some great opportunities, as you saw in heavy duty, you know, the substitute for the pipe ranch. That’s a great new product. And so we see things like that all the time. We see enhancements to our visual control system, our tool control system, which we’ve seen now. Amazingly, we’ve seen the tool control systems more and go bleed into oil and gas. We had a major sale in Canada associated with oil and gas, as opposed to when we had been using it just for aviation. We can see it rolling into railroads, so with small enhancements. That’s the kind of thing we’re doing.

Liam Burke: Great. Thanks Nick, thanks Aldo.
Operator: Our next question comes from David MacGregor with Longbow Research.

David MacGregor: Yes, good morning, everyone. Congratulations, Nick, on the good quarter.

Nick Pinchuk: Thanks.

David MacGregor: The question is on the Tools Group and just – you know, your margin’s up 150 basis points, including 60 bps of negative FX. You just come through a period where you had a couple of years of really kind of hyper growth as, you know, if that term might be applied to this particular category. That growth seems to be slowing now. Obviously, there’s a lot of cost opportunity – cost of opportunity that, you know, is out of reach when you’re getting that kind of a growth, but now that the growth is easing a little bit, maybe that cost of an[?] opportunity becomes a little more accessible. I guess the question is just, how sustainable are these kind of year-over-year margin progression numbers, given, you know, you now have a cost of opportunity that you may not have had for the last couple of years?

Nick Pinchuk: Yeah, I think there’s – I think there’s some of truth in what you say there. I don’t think you can predict quarter by quarter in this kind of situation. Of course, on one end, with your eyeballs bleeding for, you know, trying to double digit – double digit growth, you know, that kind of thing, you maybe pass up some efficiency opportunities, but we like to believe we take full advantage of those kind of things. I think though, if you look at our overall numbers, if you look at the OpCo margin growth for the corporation, and you take a look at the year-over-year OpCo margin and you go back and see it, you’ll see that it’s been triple digits an awful lot of times awfully far back, in big sales growth and small sales growth. So I think – you know, we’ve been able to – we’ve been able to grow that margin in a lot of different situations on an overall basis. Now, when you – when – in the situation of the Tools Group, it does give you a little more – a little more advantage, a little opportunity to look at that, but I wouldn’t let – I wouldn’t allow the characterization that 5.6% is slow growth. I think that’s pretty good growth. I mean, you’re talking about 5.6%
organically in GDPs that are throwing between 1 and 2 all over the world. So I think it’s pretty good.

David MacGregor: If I could just follow up with a couple of other quick ones.

Nick Pinchuk: Sure.

David MacGregor: The slower growth in the origination, how much of that was just the flat undercar?

Nick Pinchuk: Say that again, please?

David MacGregor: The slower growth in originations, I’m just wondering how much of that might have been due to lack of growth in undercar?

Nick Pinchuk: No, I don’t think it’s that much. I mean, the thing is that, of course, there’s some undercar equipment that gets sold into the Tools Group space, but you’re – primarily, when you’re talking about EC, you know, the originations, the primary driver is tool storage, and the second driver is the big ticket diagnostics, so it’s not really – there’s some of it in there floating around, but I don’t think that’s much of a factor.

David MacGregor: Okay, last question. Just, I know, we think of you as going to market through your franchisees, but you have a pretty substantial distribution arrangement as well.

Nick Pinchuk: Sure.

David MacGregor: Was de-stocking within your distribution partners – how much of a growth inhibitor was that through the quarter?
Nick Pinchuk: You know, I’m sure there was some of it, but I – you know, I’d have to say it might have been, you know, it would have shown up in the industrial business. That was flat. Like I said, it was up sequentially, you know, which gave us some positives. I don’t think it was a huge factor this quarter. It might have been some [inaudible].

David MacGregor: Okay. Thanks very much.

Nick Pinchuk: Sure.

Operator: Our next question comes from Tom Hayes with Northcoast Research.

Tom Hayes: Hi. Good morning, gentlemen.

Aldo Pagliari: Good morning.

Nick Pinchuk: Good morning.

Tom Hayes: Just kind of on the RS&I group, Nick. The organic growth rates have been kind of bouncing around the last couple of quarters. I was just wondering maybe you could provide a little bit clarity, kind of dig in to that a bit, maybe the growth trajectory of the diagnostic equipment versus the undercar that’s in there as well.

Nick Pinchuk: Yeah. Look, the – like we said in the, I think, the statements here, the formal statement is that diagnostics, information products, which is – and diagnostics too – so that would be like Mitchell and Diagnostics – the software and the handheld hardware to independent repair shop owners and managers was up mid-single-digits and it’s been up that kind of number, I think, every quarter for a long time. I can’t attest to exactly but I think it’s been – most quarters, it’s been bouncing around mid to high single-digits.
Tom Hayes: Okay.

Nick Pinchuk: So I think that’s doing pretty well. I think the big thing about diagnostics this time, I mean, not diagnostics but RS&I this time, as I tried to make clear in the quarter, we have this business in RS&I which produces, which takes contracts, OEM-commissioned contracts, to distribute — you could talk essential tools or to facilitate a project. So, for example, you might have somebody, Aldo referred to this, to do some air conditioning, provide an air conditioning reclaim system for all of its dealers. One of the manufacturers will say, ‘I want you to provide an air conditioning system, I want you to get it to my dealers, I want it to be two per dealer and I want it to be rolled out in the next four quarters or three quarters.’ We rolled it out. That’s a pretty big piece of sales business. You might have another that does an essential tool for a particular new product or a new technology that rolls out on a new truck and that rolls through in the quarter. But what happens is, these are driven by the view of the OEM and the technology and the differences that are rolling through their new models so they tend to be quite lumpy. And what happened in this quarter for that particular type of business, this was kind of a stall quarter in that business and that created the overhang in — one of the overhangs — in RS&I.

Tom Hayes: Okay. And then on the –

Nick Pinchuk: - but the stuff we sell to individual dealers was pretty good.

Tom Hayes: On the Car-O-Liner acquisition –

Nick Pinchuk: Yeah?

Tom Hayes: – well, there’s roughly 95 million of revenue. Is that – maybe just a little bit of geographic clarity, is that all Europe or is kind of a spread country market?
Nick Pinchuk: No. No. No. No. No. It’s about – it’s like this, it’s about 45% the U.S., about 30% in Europe and the rest of the world, but there’s a big piece of that, you know, like 25, 20 points to 25 points in Asia. That’s the way it works, you know. And 375 people, you know, 100 in the factories, 150 selling, 50 engineers and the rest are doing other things.

Tom Hayes: Okay. Last one, if I could, for Aldo. Fourth quarter last year on the operating expenses, it took a pretty big step down versus 3Q ’15. Is there anything in there that maybe you guys held back last year that we need to think about this year?

Aldo Pagliari: No, I mean, top of my mind, you know, the only thing I can think about that creates a little bit of volatility is if there’s changes in mark-to-market, depending on stock price movement one way or the other.

Tom Hayes: Okay. Thanks.

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

David Kelly: Good morning. This is David Kelly in for Brett. Thanks for taking my questions.

Nick Pinchuk: Good morning, David.

David Kelly: Good morning. Just a quick follow-up on RS&I, specifically the undercar business being flat. We’ve heard similar commentary from other aftermarket retailers and installers and, you know, they’ve mostly been referencing the residual impact from last year’s mild winter weather. I’m just thinking about some of the industry fundamentals and miles driven being up, you know, it feels like it’s a bit surprising that that segment is still lagging. And I guess the question is, do you
think there is some pent up demand there or some real opportunity for you as we kind of lap last winter and slowly inch to 2017?

Nick Pinchuk: Yes. I don’t know. You know, for us, the winter thing is a double-edged sword. I’ve heard people say winter is tough and therefore we don’t sell balancers or, you know, we don’t sell – we don’t do tire service, wheel service, winter is mild so we don’t do as much tire service. On the other hand, I’ve heard people say, ‘Yeah.’ People are crashing into it each other, left and right, there’s a lot of repair, you know. We need more lifts, we need more alignments going on, you know. People are running into bumpers or bouncing into potholes. So it’s a double-edged sword. I’m not so sure for us. I do think there’s opportunity in our business. What we saw there was variation from product to product. We saw kind of a stronger quarter on alignment, you know, and a couple of the other product lines were a little bit weaker. We didn’t really think it was very significant or indicative of anything actually for us. We do think there’s opportunity for the equipment business going forward though because we like our products.

David Kelly: Okay. Great. So you don’t see any real structural issue that, you know, for whatever reason undercar –

Nick Pinchuk: I don’t think so. I don’t think so. We don’t see it anyway and we’re in the garages every – you know – we have people in the garages for hours every week.

David Kelly: Sure. Sure. And then, I guess, a follow-up on the strong Tools organic growth, I was just wondering if you could talk about some of the drivers there, you know, specific product segments that are just really outperforming as of late or, you know, even regional trends, are you seeing some specific region or part of the U.S. that’s really up?

Nick Pinchuk: Right. There’s – there can be regional trends but they tend to vary quarter-to-quarter, to tell you the truth, you know. The thing is, I can tell you, I was just with a bunch of franchisees
and, you know, from all over the country. This is the National Franchisee Advisory Council. They all seemed positive and they're representing their regions, you know. So I didn't run into a single person who was saying, 'Oh, you know, I mean, it's tough, you know.' They weren't saying that. They were positive. At the SFC, I can't emphasize enough how important it is when people order more year-over-year. What it means is they're putting their money on the line, they're committing to take in product that they think things are going to be positive, so they've got a positive outlook. So we feel good about that.

What's driving our business, I think, are three, maybe three factors. One is, our new product is pretty robust. You heard me talk about a couple of them. You know, from hand tools, we got – hand tools were up in the quarter, tool storage was up in the quarter, diagnostics was up in the quarter. You talk about that product line because our – you think about it, our customer connection and innovation is better than ever before. We have more hit products than we ever had. Secondly, our franchisees are stronger. They are stronger and despite the fact they're stronger, they seem to be hungrier for more product. And thirdly, we've invested in things in the vans, like the Rock N’ Roll Cabs, the – you know, our – for the TechKnow vans. And our franchisees are so confident at taking on assistants, so that the model itself is getting better. Said another way, this is a great market. Auto repair is a great market and, like I said, every quarter, we know how to take better advantage of the opportunity. You can see it in the numbers.

David Kelly: Okay. Great. Thanks. And one more for me, and thanks again for taking my questions, I'll pass it along. You referenced that the, you know, jump into the U.S. collision market with the deal, I mean what – how do we think about U.S. collision here? I mean, my understanding is you guys didn't have a ton of exposure to that market and I know the U.S. collision sector, you know, from talks with the LKQs and the Carparts of the world, has certainly been strong and feels like it's going to be strong for the next few years. I mean, what do you think your opportunity is in U.S. collision?
Nick Pinchuk: We like it for a few reasons. One is, we believe Car-O-Liner is a great brand but when you smear the Snap-on patina over it, it’s even stronger. Secondly, this is a space which is changing. Different materials are requiring different modes of collision repair and Car-O-Liner is at the upfront on that with regard to their product line and our research and engineering can augment those 50 or 45 engineers at Car-O-Liner to make them better. Thirdly, we think that repair is starting to become more important in collision shops because there’s intelligence that’s distributed around the car. You got a dent, you’ve got to repair things. And so we can bring the repair aspect to collision shops, something no one else can do in this space. Our product in terms of our physical product and our database associated with repair. So we think it’s a great coherent acquisition.

David Kelly: All right. Great. I appreciate the call. Thanks again.

Operator: We’ll take our next question from Scott Stember with CL King.

Scott Stember: Good morning.

Aldo Pagliari: Good morning.

Nick Pinchuk: Good morning.

Scott Stember: Can we maybe talk about Brexit on your initial observations, whether you’ve seen any impact on the UK market and, you know, either from a sales or a currency perspective. And then maybe just talk about your expectations for currency, it looks like we still have some headwinds. I know, initially, before Brexit, there was a thought that later in this year that the comparisons would start to flatten out. Can you maybe just talk about those two things?
Nick Pinchuk: Yeah. Look, Brexit, of course, as I referenced, is a challenge for us. It’s part of the turbulence in Europe. But in fact, you know, if you look at the three pieces of our businesses in Europe, if you look at – if you look at the Tools Group, up strong in UK. You look at RS&I, up nicely. But you look at SNA Europe and SNA Europe was up in the quarter again. I think it was the 12th straight quarter of growth, that was down slightly. So Brexit might have hurt them a little bit. But, really – but generally, overall volume, it was a great market for Snap-on. UK was one of our better markets. The problem is in the currency. So it becomes a big dinger in terms of – it becomes a big effect in terms of sales, translation effect on our sales because we have pretty good sales in pound, and secondly, remember, we’re selling into the British market, selling in pounds but we’re making in dollars, we’re making in the United States. So we have a transactional impact. So if you step back and you look at our currency in the quarter and overall for the corporation, that $2.22, it had $0.05 of currency impact and a lot of that was the UK, a lot of that was the UK. Of course, there were some other factors in there. And then looking forward, when you start to look at it, the UK started, you know, kind of went down in the quarter. So we think, you know, it’s kind of like from a sales perspective looking forward, we probably don’t see as much pressure from translation but the profitability will be about the same, maybe a little bit more impacted going forward because of the pound. Now, going out beyond where we are now, and that’s based on where we sit today in terms of the pound, if the pound gets weaker, it will impact us more. But that’s the major factor. We think our product and our approved capabilities overwhelm the sales factor, the selling factor. It’s just the currency tends to impact us.

Scott Stember: Got it. And just a last question on weather again. Taking a different slant, the record warmth that we’ve this summer, maybe for like air conditioning related products, have you seen any jump in demand for any tools that are related to any kind of AC repair?

Nick Pinchuk: See, you know, I don’t – I’m sure that happened. But I can’t quote you any figures on that. I haven’t sliced the tools by virtue of AC repair. That is one of the things that does happen. You know, every year, there’s a new story about that, you know, it’s a hard winter or a short
winter and people have different tools to sell. But the cool thing about Snap-on is we have the widest product line. So whatever the conditions, we have something to sell into those conditions.

Scott Stember: Got it. That’s all I have. Thanks so much for taking my questions.

Nick Pinchuk: Okay.

Operator: Our next question comes from Gary Prestopino with Barrington Research.

Gary Prestopino: Hey. Good morning.

Nick Pinchuk: Hey.

Gary Prestopino: A couple of questions, did you call out what the European hand tools business was up on a percentage basis this quarter, Aldo?

Nick Pinchuk: I did not.

Aldo Pagliari: I did.

Nick Pinchuk: It’s up mid – I think, maybe we did.


Nick Pinchuk: Mid-single-digits. Mid-single-digits.

Gary Prestopino: Okay.
Nick Pinchuk: Yeah.

Gary Prestopino: So that’s how you were – that’s –


Gary Prestopino: No. I was just going to say that’s about where it’s been all year, right?

Nick Pinchuk: Yeah. It’s been – it’s been around that level. Yeah. It’s been growing. I mean, it’s still, you know, I hate to say this but it’s still got headroom. I mean, you know what, it’s still below where it was at its peak, maybe 15% or so below where it was, so we think it’s got headroom. And the profitability up 14 straight quarters, we know that has runway.


Nick Pinchuk: That’s good thing for us.

Gary Prestopino: Right. And then could you give us some idea of what Car-O-Liner’s growth had – has been historically and where you think you can take that, its top line growth?

Nick Pinchuk: I don’t think we’re looking backwards in terms of growth. We like to look forward and we see this as kind of, you know, in the five plus, you know, sort of the RS&I type. You know, when you think of the RS&I type business growth, that’s where we see it, you know, the five plus type business. You know, I think it’s a kind of a fool’s errand to be too definitive looking forward. But I can tell you that, we think, looking at it, that that’s a solid projection.
Gary Prestopino: Okay. That’s good. And then in terms of it looks like year-to-date, the corporate expenses are down about 30 million, your SG&A is down as well. Is that all dealing with the pension expense on the mark-to-market on the spot?

Aldo Pagliari: It is, Gary. The pension this year, you know, the way the accounting rules work, we have a savings per quarter of about $1.9 million. So you can multiply that by three and you get a year-to-date amount. And then noise that’s created by how the stock price moves, not just this year but remember, you have to look at the movement relative to last year. So this particular quarter, there’s really no change in mark-to-market, it’s very benign, so most of the change in corporate expenses this quarter is related solely to pension expense.

Nick Pinchuk: Yeah. And we look at it, as the quarter’s down, I think, year-over-year, like $1.2 million or something like that, $22.5 versus $23.7. But the penalty for currency was well more than offsetting that, that good news out of pension. So we think we ended up on the short end of that combination.

Gary Prestopino: Okay. That’s all I have. Thank you.

Nick Pinchuk: Okay.

Aldo Pagliari: Thank you.

Operator: We’ll take our last question from Richard Hilgert with Morningstar.

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

Aldo Pagliari: Good morning.
Richard Hilgert: All my questions have already been asked. Congratulations on a great quarter. Good to see that continued improvement in the profitability across the groups still and still seeing that nice growth in the financial services area. And I appreciated that little of color earlier on the differentiation between what’s going on in hand tools and the growth in financial services. Just the final question remaining for me was I notice that on a percentage basis, if you take a look at your intersegment number on the breakdown for revenue with the segments, it’s gotten a little bit larger compared to history. It’s running now above a 14% kind of number as a percentage of the total of the segment revenues and on an absolute basis now up to $139 million. I’m just curious what’s driving that and should we be expecting that percentage to be a higher amount of the total going forward?

Nick Pinchuk: Yeah. No. No kidding. The – it will grow because the Tools Group has been growing. You see, if you think about it, the Tools Group, it’s got its own factories but it’s got that great distribution. So, you know, inside C&I, there are factories like the power tools factory and so on like other places that sell, you know, they sell externally but they also sell to the Tools Group. SNA Europe does that. RS&I has some divisions that do that. We have torque wrenches in C&I that do that out in California, sell in both places. So as the Tools Group grows, you will see intercompany sales grow. It’s a natural outcome of that.

Richard Hilgert: Okay. Great. Thank you very much. And again, congrats on the quarter.

Nick Pinchuk: Okay.


Operator: That concludes today’s question and answer session. At this time, I would like to turn the conference back to Leslie Kratcoski for any additional or closing remarks.
Leslie Kratcoski: Thanks, everyone, for joining us today. As usual, a replay 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. Thank you for participation.