

Snap-On (SNA) Update- 3/19 Quarter

Maintain SELL

- SNA's contract receivable days rose by 3.3 over the year-ago quarter with all of the increase centered in long-term receivables. While the year-over-year pace of expansion has slowed, it appears that the company is continuing to increase credit extension to franchisees to boost sales to that channel.
- Past-due receivables stats for contract receivables improved in the quarter and led to a \$3.3 million decline in provision expense for the portfolio which we estimate provided a 4.5 cps tailwind to EPS.
- The increase in extension of credit to customers via finance receivables continued with total long-term contract receivables days of sales jumping by almost 8 days of total non-financial revenue. Total delinquencies as a percentage of gross finance receivables fell by 8 bps with all categories improving except for a slight uptick in receivables delinquent by 35-59 days.
- Inventory days of sales (DSI) increased by almost 10 days over the year-ago quarter, continuing a long trend of inventory growth outrunning sales growth.

Contract Receivables

SNA's contract receivables include amounts due from external customers, but also loans to franchisees to fund working capital, franchise and van leases, and the expansion of existing franchises. The below table shows the calculation of short and long-term contracts days of tool group sales:

	3/30/2019	12/29/2018	9/29/2018	6/30/2018
Snap-on Tools Groups Sales	\$410.2	\$407.4	\$389.8	\$411.9
ST Contract Receivables	\$92.9	\$98.3	\$105.6	\$87.6
ST Contract Days	20.7	22.0	24.7	19.4
LT Contract Receivables	\$345.1	\$344.9	\$338.1	\$332.6
LT Contract Days	76.8	77.3	79.1	73.7
Total Contract Receivables	\$438.0	\$443.2	\$443.7	\$420.2
Total Contract Receivables Days	97.4	99.3	103.9	93.1
	3/31/2018	12/30/2017	9/30/2017	7/01/2017
Snap-on Tools Groups Sales	\$404.7	\$409.2	\$392.7	\$413.8
ST Contract Receivables	\$92.0	\$96.8	\$99.8	\$82.4
ST Contract Days	20.7	21.6	23.2	18.2
LT Contract Receivables	\$326.1	\$322.6	\$310.4	\$299.4
LT Contract Days	73.5	71.9	72.1	66.0
Total Contract Receivables	\$418.1	\$419.4	\$410.2	\$381.8
Total Contract Receivables Days	94.3	93.5	95.3	84.2

Short-term contract days were flat with the year-ago level while long-term contract receivable days were up by 3.3 days. While the pace of the year-over-year expansion in contract receivable days has slowed, it appears that the company is still utilizing credit expansion to fund sales to franchisees.

On a positive note, the trends in past due contract receivables improved in the quarter:

Contract Receivables	3/30/2019	12/29/2018	9/29/2018	6/30/2018
30-59 days past due	0.29%	0.38%	0.40%	0.47%
60-90 days past due	0.20%	0.27%	0.31%	0.21%
>90 days past due	<u>0.32%</u>	<u>1.16%</u>	<u>0.85%</u>	<u>0.82%</u>
Total past due	0.81%	1.81%	1.56%	1.51%
>90 Days and Still Accruing	0.09%	0.04%	0.04%	0.05%
Contract Receivables	3/31/2018	12/30/2017	9/30/2017	7/01/2017
30-59 days past due	0.38%	0.28%	0.34%	0.36%
60-90 days past due	0.21%	0.14%	0.17%	0.21%
>90 days past due	<u>0.57%</u>	<u>0.45%</u>	<u>0.41%</u>	<u>0.44%</u>
Total past due	1.16%	0.87%	0.91%	1.01%
>90 Days and Still Accruing	0.09%	0.14%	0.14%	0.18%

This paved the way for a \$3.3 million decline in provision expense in contract receivables which would have added about 4.5 cps to EPS in the quarter.

Finance Receivables

SNA's finance receivables include financing to external customers which includes financing to franchisee customers. We will use total non-financial sales in our calculation even though sales to franchisees does not provide an exact timing match to actual sales made to franchisee customers.

	3/30/2019	12/29/2018	9/29/2018	6/30/2018
Sales	\$921.7	\$952.5	\$898.1	\$954.6
ST Finance Receivables	\$525.9	\$518.5	\$519.0	\$514.4
ST Finance Receivables Days	52.1	49.7	52.7	49.2
LT Finance Receivables	\$1,077.1	\$1,074.4	\$1,058.3	\$1,051.3
LT Finance Receivables Days	106.6	102.9	107.5	100.5

	3/31/2018	12/30/2017	9/30/2017	7/01/2017
Sales	\$935.5	\$974.6	\$903.8	\$921.4
ST Finance Receivables	\$512.2	\$505.4	\$505.8	\$496.5
ST Finance Receivables Days	50.0	47.3	51.1	49.2
LT Finance Receivables	\$1,035.9	\$1,039.2	\$1,018.6	\$998.6
LT Finance Receivables Days	101.0	97.3	102.8	98.9

The above table shows that short-term finance receivable days rose by 2.1 days over the year-ago level while long-term finance receivable days jumped by 5.6 days. This is the third straight quarter of substantial increases in long-term finance receivables relative to revenue growth and indicates the company is still utilizing credit extension to drive its sales growth.

The below table shows delinquency trends in the finance receivable portfolio:

Finance Receivables	3/30/2019	12/29/2018	9/29/2018	6/30/2018
30-59 days past due	0.85%	1.17%	1.08%	1.04%
60-90 days past due	0.58%	0.73%	0.74%	0.65%
>90 days past due	1.17%	1.23%	1.19%	1.00%
Total past due	2.60%	3.13%	3.00%	2.69%
>90 Days and Still Accruing	0.90%	0.96%	0.94%	0.76%

Finance Receivables	3/31/2018	12/30/2017	9/30/2017	7/01/2017
30-59 days past due	0.82%	1.21%	1.01%	0.99%
60-90 days past due	0.62%	0.87%	0.73%	0.63%
>90 days past due	1.25%	1.26%	1.22%	0.94%
Total past due	2.70%	3.33%	2.97%	2.57%
>90 Days and Still Accruing	0.98%	0.96%	0.98%	0.72%

Total past due receivables as a percentage of the total portfolio fell by 8 bps with a slight uptick in receivables past due in the 30-59 day range which is not a material concern at this point.

Inventory Continued to Increase

SNA's inventory growth has been outrunning growth in sales for some time. After adjustment for a \$20.9 million increase in inventory from the adoption of ASC 606 at the beginning of 2018, we estimate days sales of inventory in the 12/18 quarter was about 6 days ahead of the year-ago period. Management was asked in the fourth quarter conference call if the company had too much inventory:

“No, no. I wouldn't say were over-inventoried in big-ticket merchandise. I would say that we're adding a lot of tools. We added 5,000 different line items for Industrial last year. So, we'll keep adding to tools.”

“Now, you can say okay we are not getting all the sales we want. But if you look at the trajectory of our businesses, if you look at near-term maybe and get in a twist, but if you look at the trajectory of the Tools group over a five, six years, you'll see that it's more than 5%.”

Nevertheless, the increase in inventory continued into the 3/19 quarter with DSIs rising almost 10 days over the 3/18 quarter. We realize that inventory is likely being inflated by

rising raw materials prices and higher growth in more expensive diagnostics equipment will also have an effect. However, a 10-day jump on the back of a sustained trend of rising DSIs is concerning.

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