Snap-On (SNA)

Updated July 20th, 2018 by Josh Arnold

Key Metrics

Current Price:	$173	**5 Year CAGR Estimate:**	10.3%	**Quality Percentile:**	31.8%
Fair Value Price:	$177	**5 Year Growth Estimate:**	8.0%	**Momentum Percentile:**	59.0%
% Fair Value:	98%	**5 Year Valuation Multiple Estimate:**	0.4%	**Valuation Percentile:**	65.3%
Dividend Yield:	1.9%	**5 Year Price Target**	$260	**Total Return Percentile:**	69.0%

Overview & Current Events

Snap-On Tools was founded in the early 1920's and since that time has grown from a fledgling direct sales distributor of sockets to a full-service, global distributor of a wide array of common and specialty tools. The company's market capitalization is $9.8 billion, and it should generate almost $4 billion in revenue this year.

Q2 results were reported on 7/19/18 and the stock moved up nearly 10% on the news. Revenue gained almost 4% through a combination of organic and inorganic (acquisition-based) growth. Commercial and Industrial led the way, offsetting relative weakness in the core Snap-On Tools segment. The financial services segment produced higher revenue and margins, with the broad-based strength leading to 20% earnings-per-share growth in Q2. We've slightly raised our estimates for 2018 earnings as a result of the strong report.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$4.07	$2.32	$3.19	$4.50	$5.20	$5.93	$7.14	$8.10	$9.20	$10.12	***$11.70***	***$17.20***
DPS	$1.20	$1.20	$1.22	$1.28	$1.36	$1.58	$1.85	$2.20	$2.54	$2.95	***$3.28***	***$5.65***

With the exception of 2009, Snap-On has produced materially higher earnings every year in the past decade. The company's constant focus on acquisitions as well as its own organic revenue growth in concert with a rapidly growing financial services business have created a growth picture that is tough to rival. Snap-On's enormous breadth of its catalog – created largely through acquisitions over the years – makes it a true global leader in its industry. The company continues to buy back its own shares as well, providing another tailwind for earnings-per-share. We see 8% earnings-per-share growth annually going forward as Snap-On continues to acquire brands, produce low single digit organic growth, see a low single digit tailwind from buybacks, and small gains from its cost saving program; it will see a bump in earnings this year from a lower tax rate as well. Growth of 8% a year would represent a slowdown from Snap-On's historical rate of growth, but based upon slowing rates of revenue growth, we believe this caution is warranted.

We see the dividend continuing to move higher at double digit rates, continuing Snap-On's track record of payout growth from recent years. Management is committed to making Snap-On a premier dividend growth stock and with the payout ratio still low and earnings growth rates in the high single digits, there is plenty of room for it to move higher.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	12.1	14.2	14.4	12.3	12.7	15.6	16.8	19.1	17.1	16.3	***14.8***	***15.1***
Avg. Yld.	2.4%	3.6%	2.7%	2.3%	2.1%	1.7%	1.5%	1.4%	1.6%	1.8%	***1.9%***	***2.2%***

Snap-On's price-to-earnings multiple has spent the past several years in the mid-teens and today, it is 14.8. The recent rally in the stock has sent the valuation back near our estimate of fair value, which is 15.1 times earnings. As a result, we see just a 0.4% tailwind to total returns from the valuation as the stock has rallied significantly since our last report.

We see the yield remaining near where it is today as the share price and dividend growth should roughly mirror each other. Snap-On isn't an income stock with the yield at just 1.9%, but it is a very strong dividend growth issue and will remain so for the foreseeable future, increasing its attractiveness for dividend growth investors.

Disclosure: This analyst has no position in the security discussed in this article, and no plans to initiate one in the next 72 hours.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	43.8%	43.7%	46.8%	46.9%	47.3%	48.2%	48.3%	49.2%	49.8%	49.5%	***49.6%***	***49.8%***
Debt/A	56%	62%	62%	58%	53%	48%	48%	44%	44%	43%	***42%***	***40%***
Int. Cov.	14.4	5.5	6.2	8.0	9.3	10.5	13.0	14.8	16.5	16.8	***17.0***	***20.0***
Payout	29%	51%	38%	29%	27%	26%	26%	27%	27%	28%	***28%***	***33%***
Std. Dev.	52.7%	54.9%	23.3%	31.7%	18.4%	11.6%	17.1%	14.2%	21.4%	15.6%	***19.0%***	***26.0%***

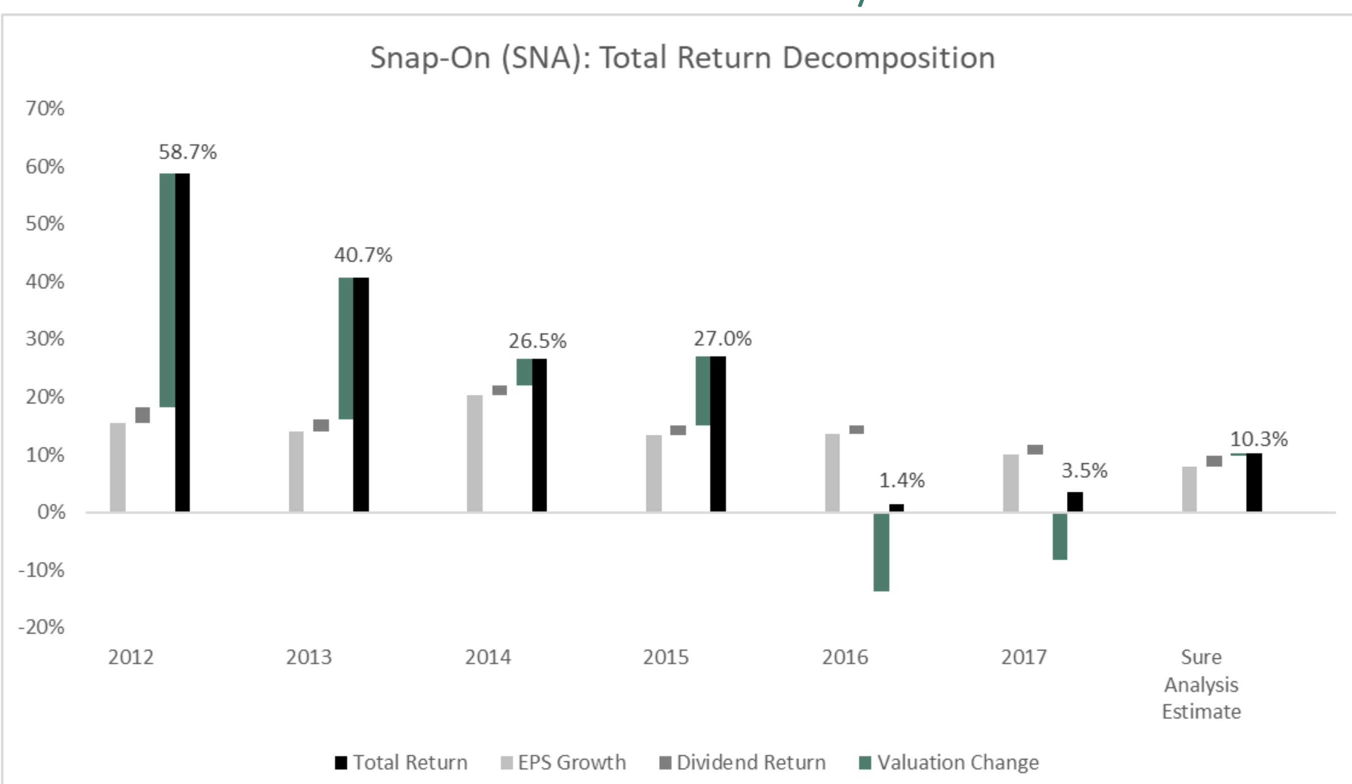
Snap-On's quality metrics have improved slightly over the past decade as its margins ticked higher, but seem to have plateaued, while debt has come down and interest coverage has improved. The company's focus on margin improvement is surely the result of three years at 49% gross margins and should help a bit with further growth. Financing certainly is of no concern for Snap-On given its pristine balance sheet as well as its high rates of profit growth. The payout ratio is still very low and should remain in the low-30% range unless management decides to ramp up its dividend growth strategy, which we view as unlikely at this point given already-strong growth rates. Overall, Snap-On is in terrific shape financially.

Its main competitive advantage is in its very broad and deep assortment of all kinds of specialty tools. In addition, its global reach and in-house financing is a unique combination not found elsewhere. The financing business could pose a problem during a recession as customers may become past due on their accounts, so this would be the principal risk for Snap-On during the next economic downturn. Indeed, earnings suffered mightily during the Great Recession.

Final Thoughts & Recommendation

After two years of below market total returns, Snap-On was significantly undervalued. However, the recent rally has taken it back near fair value, so our estimate of projected returns has come down. We now see total annual returns of 10.3% going forward, consisting of the 1.9% current yield, 8% earnings growth and a 0.4% tailwind from the valuation. Snap-On has been able to produce strong growth for many years consecutively and its focus on buybacks, acquisitions and margins should continue that streak. Snap-On looks suitable for both growth and dividend growth investors.

Total Return Breakdown by Year



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