FINAL TRANSCRIPT

Thomson StreetEvents℠

SNA - Q3 2008 Snap-on Incorporated Earnings Conference Call

Event Date/Time: Oct. 23. 2008 / 10:00AM ET

CORPORATE PARTICIPANTS

Marty Ellen
Snap-on Incorporated - SVP, Finance & CFO

Nick Pinchuk
Snap-on Incorporated - President and CEO

CONFERENCE CALL PARTICIPANTS

Jim Lucas
Janney Montgomery Scott - Analyst

Alexander Paris
Barrington Research - Analyst

David Leiker
Robert W Baird - Analyst

PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the 2008 third quarter results conference call, hosted by Snap-on Incorporated. At this time all participants are in a listen-only mode. At the conclusion of our remarks, we will conduct a question and answer session. (OPERATOR INSTRUCTIONS) As a remainder this call is being recorded.

I would now like to introduce your host for today's conference call, Marty Ellen, Chief Financial Officer. You may begin your conference.

Marty Ellen - *Snap-on Incorporated - SVP, Finance & CFO*

Thank you, Shawn, and good morning, everyone. Thank you for joining us today to review Snap-on's third quarter 2008 results. By now you should have seen our press release issued this morning. Despite increased challenges in the economy, we believe that our third quarter results demonstrate our continued progress in our core strategic and operating initiatives. We'll success these with you today. Joining me is Nick Pinchuk, Snap-on's President and CEO. Nick will kick off our call this morning with his perspective on our business and results. I will then provide a more detailed review of financial results and afterwards we'll take your questions. Consistent with past practice, we will use slides to help illustrate our discussion. You can find a copy of these slides on our website next to the audio icon for this call. These slides will be a 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 (inaudible) managements or the companies outlook, plans, or projections, are forward-looking statements and actual results may differ materially from those made in such statements. Additional information in the factors that could cause our results to differ materially from those in the forward-looking statements are contained in our SEC filings this call is copyrighted material by Snap-on Incorporated. It is intended solely for the purpose of this audience. Therefore it cannot be recorded, transcribed or rebroadcast by any means without Snap-on's expressed permission. With that said, I will now turn the call over to Nick. Nick?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Thanks. Well, it appears we live in an interesting times. Uncertainty seems to be the order of the day. And of course Snap-on is not immune. But what you can still depend on is that enabling solutions, real products for critical jobs, continue to be in demand. Even now. And thats what Snap-on is all about. So, whats also reliable, even in these times, is the strength of our corporation's business model, the breath of our customers, the power of our value creating processes, and of course, most importantly, the capability and commitment of our team.

In this past quarter, those extraordinary characteristics were on display again. Sales growth was a lot tougher but the strength of our brands and the pull of new innovative products provided, what I think was, significant buoyancy. All of that combined to create record earnings for the quarter. Operating margins expanded 170 points to over 12%. EPS of $0.94 is a record for any third quarter, any time, in the history of our corporation. And for the nine months completed so far this year, operating margins reached 13%. Now, those of you who have been listening to us for some time might recall that this was the very goal we set for ourselves a couple of years ago. It was a goal we thought would be achieved but we thought it would be achieved in 2010. So, we are ahead of our own targets despite the macro economic difficulties. Now, I will be giving you some more specifics as we go forward, but before I do, I have to note -- I want to note, that we could not have accomplished this past quarter's performance without the extraordinary efforts of all our associates and franchisees. I know many of you are listening in today to what is your call. My congratulations and my thanks to each and every one of you.

It's clear that these are turbulent times. There's significant uncertainty for both businesses and individuals and as I've said many times, Snap-on is not immune. But we're fully aware of the difficulties and we're vigilant regarding the potential impact and the need to act against eventualities. But having said that, we believe our strategies and business models do create resiliency. We have a growing global position with an expanding presence in emerging markets. We benefit from a diverse set of professional users in critical industries from vehicle repair to aerospace to natural resources to alternate energy. Those are fairly favorable places to be in difficult times. Places where Snap-on products fill crucial needs and enhance productivity and in the end make money for our customers. Beyond that we hold some of the strongest brand positions anywhere and underpinning all of this is our value creation approach with differentiating processing like rapid continuous improvement, enabling innovation and passionate customer care.

So, having said that as an overview, let me give you some highlights of our results. This year for the nine months almost 45% of our sales were outside the US. That compares to about 42% for the same period just a year ago. And about 8% of sales, our global sales, are now in the emerging markets of Asia Pacific and Eastern Europe. Now, if you look at international in a broad sense, the slow down of Western European economies and the generally tighter credit conditions did make it even more challenging this quarter for both our S&A Europe tools business and for our European based equipment operations. But the rest of our international businesses remain strong contributors throughout the period. Even the casual attention to the media, I think today, would lead you to question the global economy. Well we still see opportunity and runway. So, we're continuing to invest in emerging markets. Progress continues on our next -- our third plant expansion in Kunshan, China. We're already producing power tools and undercar equipment and hacksaws in that location. Now, we're adding a third facility supporting new products for Asia, like bansaws and tool storage. We're continuing on schedule with that project and we expect to be up and running in about six months for both of those product lines. And the first quarter acquisition of our 60% interest in (inaudible) Snap-on is also proceeding well. That new venture is providing what consider to be high quality, hot forged, hand tool capacity for our markets throughout the world.

Now, let's talk for a moment about eastern Europe. I don't know that we've highlighted that region as much as we might have, but we continue to see growth opportunities in those unclaimed markets and we're moving forward successfully with the relocation of our plant in [Belarus]. I think I mentioned last quarter that that facility makes important cutting tools and they're low cost and very high quality. So, we're looking forward to expanding those capabilities as we go forward. Eastern Europe is a strategic growth region for us. Sales there are starting to be significant and they grew in the quarter by almost double digits and thats excluding currency. We're excited about the growth prospects in Eastern Europe and we're going to keep investing. Overall, about emerging markets there's still an awful lot for us to achieve. We're only scratching the surface. So, we're going to keep investing, keep pursuing the opportunities aggressively.

Now, turning to slide six, now let's talk about our markets and our customer base. We feel we are in an encouraging position. For vehicle repair technicians, remember they're served by our Snap-on tools distribution channel, (inaudible). With those customers we remain the leader, the aspirational brand of choice. This is clear, and thats a relatively long wave segment. At this point we see a mixture of both head winds and tail winds. For example, fuel prices have begun to decline. Thats probably the one bright spot in the macro economic situation, but that will lower costs for our franchisees and it will possibly dampen what we're seeing to be the downward trends in miles driven. But in addition for that segment, government data through August continues to report an increase in household spending on vehicle repair. I guess thats not surprising given the dramatic decline in new car sales. Think of it this way -- as I believe I've said before, almost 40% of the car park in the United States is now older than 10 years and its getting older. So, increase spending on repair seems logical and it seems right. Beyond the vehicle age though, I also think you -- we must consider that much of US driving is not discretionary. So, with the age and discretionary -- and the not discretionary nature of the driving, we would expect repair to remain somewhat resilient even in the face of economic slow down and thats what we're seeing. With all of that said however, technicians are certainly exposed to the uncertain atmosphere. We expect that both technicians and garage owners to be more cautious in their spending and its played out -- it appears to be so. It's not a surprise that the sales of higher priced tool storage products were again soft and the volume of our larger diagnostics products in the United States was down in the third quarter. So, just as I said -- but overall -- overall, technicians are still spending on the innovative tools that make them money. We'll speak in that context later when we talk about power tools and some of the innovations that we've brought to market in that product line. So, just as I said, the US auto market -- some head winds, some tail winds, but all in all one of the more reliable segments of the day.

Let's talk about the tools group. We're pleased this quarter that we did have a slight uptick in the US van count both versus 2007 and on a sequential basis versus last quarter. Significantly this is the first year-over-year improvement in some time so we're encouraged. But while we like to fill -- we like to fill the open territories even faster, we're being selective in recruiting. We believe that's been the right thing to do. It's lowered new franchisees terminations and reduced termination costs. That has been a help. Selectivity not withstanding though, we continue to recruit actively and we expect further increases in van count in the fourth quarter.

Let's talk about our franchisees for a minute. We believe the outlook does remain positive. In early August, we had a US franchisee conference in Las Vegas. I spent three days with many of the almost 2,000 franchisees attending and I have to tell you their attitudes were positive and they were quite excited about our new product line up. In fact, future orders from that get-together, vastly exceeded our expectations. Even in August though, we recognized the need to help the franchisees offset cost pressures. So, a significant portion of that convention, that colloquium, was dedicated to raise van efficiencies, dedicated to improving items like fuel costs, selling methods and communications charges. The training I have to tell you, was enthusiastically received and we think its working and we are confident it will serve us well going forward. Despite the convention's success however, we need to be mindful that more economic uncertainty has arisen since early August, so we're cautious at least for the fourth quarter for our US franchisee business. While the US business saw a decline in the quarter, the results were very different for the franchisees in Canada, the UK and other international franchise operations. In those jurisdictions, we achieved growth of almost 10% driven largely by innovation. A number of new product launches in areas like diagnostics and power tools. All of them had significant success in moving the technicians to purchase.

Let's talk about industrial -- our industrial business. Our focus remains on critical customer segments like the military, aerospace, natural resources, alternate energy and automotive vocational training. We're rolling the Snap-on brand out of the garage and it's working. Growth did slow from 21% last quarter to about 3% the past period. But year to date it's 14%. And we believe the variation over the last two quarters was influenced strongly by customer order timing and a strike at one of our large customers. But I can tell you order activity for industrial is now very strong, so, we expect a return to double digit growth in the fourth quarter. We're positioning to serve the tool -- tool storage and control needs of great opportunities like the expanding natural resources sector and the new major airframes being introduced around the world. We continue to invest in industrial product and resources to support that business and we see abundant runway going forward in that area and we're going to take full advantage. We're determined to do it. To the more challenged business in the quarter were our European tools business and our worldwide equipment business. At S&A Europe, while the market coverage is fairly broad base across Europe, the operation has some concentration in Southern Europe, particularly in Spain, where sales declined in the quarter by 20%. That country's economic conditions which are probably the worst in Europe -- while the country economic conditions have slowed throughout the regions, Spain has been weaker than most. And thats resulted in a challenge for S&A Europe. In the global equipment business, which sells larger priced capital goods, sales were down 5% without currency. Thats not unexpected in this tight credit environment. But even though the sale of the environment has become more challenging, we're continuing to advance our technology. Over the last few years, product innovation has been the key to significant improvements we've seen in equipment, and thats continuing. In this past quarter we introduced our Prism, imaging alignment system, which won Motor Magazines top 20 tool award. Sales driven by Prism are exceeding -- sales by Prism, are exceeding expectation, despite the overall downturn and volume in the Bell Weather imaging aligner category for equipment was up significantly. So, in equipment we're continuing to innovate and as a result we're advancing penetration of our targeted key accounts. And despite the softness we believe we're gaining market share, although its in a weak market.

Also in the C&I segment, let me talk for a moment about automotive power tools. They had a terrific quarter and it aided the franchise business significantly. Sales improved almost 34% and this is just another innovation story. Our new MG725 pneumatic impact wrench and our [CT4410] cordless impact both are powered (inaudible) leaders and have and continue to be enormous success. So, as with our equipment business, power tools had a string of successful new product launches and we had a solid pipeline of new products coming to us over the next few quarters. We've consistently said, I think, that for technicians, power tools are an essential purchase. They translate into immediate productivity and therefore will do well in a softer environment. So far this appears to be the case. The diagnostic and information group also had an encouraging quarter, considering the market for bigger ticket items. The European diagnostics business expanded in the period and our OEM facilitation won an essential tool deployment in North America that significantly aided its third quarter. Now, while business solution sales did decline, much of that was expected as a result of exiting small peripheral lines of business. Activity in the [SBF], the Snap-on business solutions core, however, was favorable in the quarter. In total, for the group, from the diagnostics and information group from a profitability perspective, that organization achieved an operating margin of 17.5% and the profits represented a growth of over 20% for the quarter.

Now let's turn to slide seven. We continue -- and I think this is important, because its authored our success for many quarters, we continue to drive improvement across our business. We drive it with a suite of strong and critical processes. We call those activities Snap-on value creation. It helped author our third quarter and it will drive further improvement going forward, we're confident. I've already mentioned a few of the innovations, while there are many more across all of the businesses. But we're going to keep investing in innovation. In fact next month we'll be opening another Snap-on innovations center right here in Kenosha. We call it the Snap-on innovation works. It will include areas to observe customers interacting with products, a modern auto repair garage. Space for both two and three dimensional prototyping and an area specifically devoted to the critical industries I talked about before. I look forward to many of you visiting. And when you do, you're going to get a first hand view of Snap-on innovation taking shape. Another process thats important to us and crucial to us is rapid continuous improvement or RCI. It also -- its played a major role in our progress. We see its results almost everywhere from manufacturing to administration to product design. For example, our COT in our US distribution business continues to perform in the mid 90s range. And while thats good and much improved over just a short time ago, we need to make it better and we will. From a productivity view point, RCI has enabled us to raise sales per associate by over 8% and in the past quarter we did see more than $10 million of commodity cost inflation. But those increases were substantial. But they were more than offset by our RCI activities. While the commodity price increases are softening going forward, we still feel, I believe that fourth quarter costs for steel freight packaging and other items will increase by about $12 million. But we're confident that we can also achieve offsets through RCI just as we have done so far.

So, while economic difficulties clearly increased in the third quarter, I think you can say that the Snap-on team met those challenges and prevailed. Sales were tougher to come by but we continue to seize opportunities in those places where growth was made available by our diversification. We continue to innovate, stimulating demand even in the face of economic weakness and we continued to aggressively deploy RCI, further improving processes and reducing costs. And while inventories have risen somewhat, there were clear purposes for that positioning. We believe that some of that paid off in capturing additional businesses in emerging markets and with selected customers. That drove up our return on capital. Having said that though some was aimed at sales that didn't materialize and we'll begin correcting for that in the fourth quarter. So, as I said, we also -- as I said, the fourth quarter was a strong quarter. Our business models, our brand, our innovation prevailed -- again economic difficulties. Now, I have Marty here to give you some of the details.

Marty Ellen - *Snap-on Incorporated - SVP, Finance & CFO*

Thanks, Nick. Turning to slide nine, net sales of $698 million in the quarter were up 2.5% from last year. Without currency, sales were up just under 1%. Clearly this was a much tougher quarter in terms of sales growth. In the US sales were up 1.3%. Our US franchisee business comprising 26% of this quarter sales was down 0.3%. Our US industrial business grew 2.8% in the quarter, substantially less than the 21% growth last quarter. We believe a substantial amount of this variation over the last two quarters resulted from timing of customer order activity. We believe this business will return to double digit growth in the fourth quarter. In Asia Pacific and the developing economies of Eastern Europe, which comprised about 8% of sales, reported growth was relatively robust at 15.3% and it was 9.1% without currency. However, in Western Europe, which comprised about 27% of this quarters' sales, our commercial and industrial tools and undercar equipment businesses faced increased headwinds due to the slowing economies. Spain and Italy have experienced some of the more severe slow downs and our S&A Europe tools business does have some concentration of its business in these countries. And as many of you already know, our equipment business which sells more expensive capital equipment and has a reasonable presence in Europe, faced the challenges of not only economic slow down but tighter credit conditions. A continuing bright spot in Europe is our UK franchisee business which had another solid quarter reporting 13.5% growth without currency. Consolidated gross profit of $312 million represented 44.7% of sales and improved 50 basis points over last year. Higher price realization along with $5.2 million of benefits from RCI initiatives, more than covered steel, freight, and other product cost inflation. Partially offsetting these improvements in gross margin was less favorable US sales mix in the Snap-on tools group. Lower restructuring costs this year of $2.2 million also benefited the gross margin rate. Operating expenses of $230.6 million in the quarter declined to 33% of sales compared to 34.4% last year. Major cost improvements were achieved through $6.4 million of benefits from ongoing RCI initiatives and $2.6 million of lower franchisee termination costs. Financial services contributed $4.8 million of operating income compared to $5.6 million last year. I will cover financial services in more detail in a moment. Operating earnings of $86.4 million for the quarter were up 19.3% over last year. As a percent of total revenues, operating earnings improved to 12.1%, up 170 basis points from the 10.4% earned a year ago. For the nine months this year we achieved an operating margin of 13% and believe we have opportunities for further margin expansion. Interest expense in the quarter is down $4.8 million from 2007, primarily as a result of lower interest rates on our floating rate debt and lower average debt levels. With the recent rise in short term interest rates, we expect interest expense will be about $8.5 million in the fourth quarter. Our effective income tax rate on earnings before equity earnings and minority interest is 33.3% in the third quarter and we anticipate that for the full year we will remain at this rate. Diluted earnings per share of $0.94 in the quarter were up 34.3% from the $0.70 earned last year.

With that as a consolidated summary, I will now turn to segment results. Starting with the commercial and industrial group on slide ten.. Segment sales of $338.1 million in the quarter were up $10.2 million, or 3.1%, over 2007. As I just mentioned, our European tools and worldwide equipment businesses experienced sales declines. Those larger businesses on a combined basis had relatively flat reported sales, but growth was down 5.6% on a constant currency basis. However, higher sales of tools kits and tools storage products to US industrial customers increased sales of power tools and continued growth in Asia and in Eastern Europe, resulted in an overall reported segment sales increase of 3.1% and a less than 1% decline without currency. Not withstanding the challenging sales environment, third quarter operating earnings of $40.7 million for the segment were up 24.5% from prior year levels, including $4.9 million of savings from RCI and cost reduction initiatives along with contributions from higher pricing. Restructuring costs were lower by $1 million. As a percentage of sales, operating earnings in the C&I segment improved 200 basis points in the quarter to 12% from 10% last year.

Turning now to slide 11, the Snap-on tools group reported third quarter sales of $269.5 million, which was up $7.5 million, or 2.9% from last year. The group's international operations again reported double digit growth. And despite the continued economic head winds in the US, sales in our US franchise operation were relatively flat, as I said down 0.3%. While van count actually improved slightly, both on a sequential and year-over-year basis. Third quarter operating earnings for the Snap-on tools group grew 14.6% from last year. Operating earnings benefited from the higher international sales volumes but this was tempered by less favorable US product sales mix. Pricing improvements, net of commodity costs increases, were about neutral for the quarter. Operating earns improved as a result of $2.6 million of RCI savings and $2.6 million of lower franchisee termination costs consistent with the lower level of franchisee terminations. As a result of these factors, operating earnings in the quarter, improved to 10.5% of sales, compared to 9.4% last year. For the diagnostics and information group which is shown on slide 12, third quarter sales of $155.1 million were up $3.1 million from prior year. Our OEM facilitation business in North America fulfilled an essential tool program in the quarter. We also achieved increased sales of diagnostics products in Europe and higher sales of Mitchell One information products. These increases were partially offset by lower US sales of diagnostics and lower activity at Snap-on business solutions resulting from the planned exit of certain non-core business lines. Operating earnings of $27.2 million for the segment improved $5 million or 22.5% from 2007, primarily due to $4.1 million of savings from RCI initiatives. As a percentage of sales, operating earnings in the quarter improved 290 basis points year-over-year from 14.6% last year to 17.5% this year.

Turning to slide 13 financial services revenues increased nearly 14% year-over-year on higher originations and in our US Snap-on credit business, revenue growth was aided by an approximate 180 basis point reduction in the year-over-year discount rate on extended credit contracts sold. Many of you have recently asked about the credit quality of the portfolio of Snap-on credit loans to technicians, so, let me give you additional data and trends. Accounts 60 plus days delinquent at the end of September, were about 1.9%. At the end of 2007 and 2006, they were about 2%. The high water mark was about 3% at the end of 2005. Not reflective of credit deterioration, but of higher franchisee turnover and consolidation of Snap-on credits field organization. For years prior to 2005 and going all the way back to 2001, the highest level experienced was about 2.2%. We believe this demonstrates the discipline, strength, and tight integration of our Snap-on credit and franchisee distribution businesses. While operating earnings and financial services were down year-over-year for the quarter, this had nothing to do with their core credit operations. We incurred $1.4 million of one-time expenses primarily related to an information systems project.

Now, let me turn to a brief discussion of our balance sheet and cash flow. As seen on slide 14, our accounts receivable increased $19.3 million from year end levels primarily due to higher levels of sales and receivables outside of the United States. Not withstanding generally longer payment terms outside the US, days sales outstanding of 73 days was equal to last year. All of our businesses are being extra vigilant in managing customer credit in this environment. Inventory performance has been somewhat disappointing with inventory turns declining from 4.9 times at last year end to 4.5 times currently. Of the nearly $66 million inventory increase over the nine month period, we believe about $20 million or so is the result of lower than expected sales. The remainder includes higher material and other cost increases, plant builds ahead of certain production line relocations and some seasonal build for school programs and other specific fourth quarter sales initiatives. As Nick said we've already begun addressing this inventory position. And even with the added level of working investment, pretax return on invested capital continues to improve. For the trailing twelve month period ended September, it was 22% and for all of calender year 2007, it was about 20%. For the comparable September 2007 period it was 18.4%. Our net debt position at the end of the quarter is $397.6 million. Our net debt to total capital of 22.4% is down from 24.9% at year end 2007. Our liquidity position remains strong. Besides the cash flow generated from operations we currently maintain a $500 million revolving credit facility provided by a strong diversified group of international banks and another $20 million of committed bank lines. All $520 million of this borrowing capacity is not presently used and our revolver does not expire until August 2012. Our current (inaudible) short term credit rating also allows us to access the commercial paper market should we need to do so. We presently have no commercial paper outstanding.

Turing to slide 15, cash provided by operating activities was $20.4 million or $39 million lower than the third quarter last year. The primary reason for this decline relates to the inventory build I just mentioned which amounted to about $23 million for the quarter as well as other timing differences primarily related to accounts payable and accrued liabilities. This concludes my marks on our third quarter performance.

Now, I would like to briefly review with you some financial considerations for the balance of 2008, which are shown on slide 16. Regarding full year 2008, we expect to continue to invest in our growth initiatives, including further investments in Asia and other global emerging, markets while aggressively managing costs. We also expect to continue implementing our other strategic and RCI initiatives, intended to enable higher levels of growth and profitability. We anticipate full year 2008 restructuring costs to be in a range of $12 to $14 millions and we expect capital expenditures to be in a range of $60 to $65 million. And as I said we also expect our 2008 effective income tax rate to approximate 33.3%. And finally we expect earnings will improve over 2007 levels for the balance of the year. Before opening the call for questions, Nick would like to provide some final thoughts. Nick?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Thanks, Marty. I just like to end by once again noting that the third quarter represented a significant increase in earnings and it was a record despite the difficult environment. I want to once again thank our associates and franchisees for making that happen. Congratulations. I also would like to end by saying that we're confident of our business models, of our runway, and of our people. Having said that it's clear that the current economic volatility is rendered projection, I think, less certain. And so as (inaudible) with such situations, we're taking action now to reduce costs, to restructure, and to accelerate productivity. As I said on practically every call, the opportunities for such improvement on Snap-on are abundant and we're increasing our emphasis on cost. It's helped us so far and it'll continue to help us in the future. But at the same time, we also continue to see opportunity. Opportunity in emerging markets. In innovative products and in critical industries. Places where working people need real solutions to crucial tasks. So, we're continuing to pursue those opportunities even in these difficult times. So as we move into the fourth quarter we know no one has great visibility in this environment. But for Snap-on, we will maintain our core strategic initiatives. But at the same time we're confident we have the flexibility and the options to shift a balance -- or to balance among the areas of sales growth, cost reduction, working capital utilization and capital investment. We're confident our operations can create a focus appropriate to the economic and business environment as it unfolds. So, as a result, we believe that Snap-on can continue its trend of encouraging progress as we go forward to the days and the years ahead. Now, we'll turn the call over to the operator. Operator?

QUESTIONS AND ANSWERS

Operator

Certainly. (OPERATOR INSTRUCTIONS) We will go first Jim Lucas of Janney Montgomery Scott.

Jim Lucas - *Janney Montgomery Scott - Analyst*

Thanks good morning guys.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Good morning, Jim.

Jim Lucas - *Janney Montgomery Scott - Analyst*

First question, could you expand a little bit on restructuring? Thats going come in just a little bit lower than a anticipated earlier in the year and how you're going to approach restructuring as you think about whats clearly becoming an even more challenging environment?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, a couple of things. One is we've said all along that yes our formal restructuring numbers are lower year-over-year but we have a number of smaller actions which have served us well in productivity and cost reduction that don't necessarily qualify for restructuring in the classical sense. And thats driven our cost reduction going forward. If you look at our numbers going into the fourth quarter, we're going to look hard at the capacity of our facilities and improving administration in terms of productivity. I think it's just doing, Jim, what we've been doing all along. If you look at our numbers we've been making some pretty good headway out of relatively -- I don't want to say flat sales but modest sales increases. So, I think you're going to see us doing that going forward, I think the only thing about this current situation is we've kind of got our alert up about trying to make sure that we match our capacity and our capabilities to the volumes as we see them.

Jim Lucas - *Janney Montgomery Scott - Analyst*

Okay. Fair enough. I mean thats exactly the point I was looking for.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

I mean, I think you're going see us taking a look at plants. You're going to see us look at a lot of things. But it's not much different than we've done before. Maybe we ratchet it up because of the current uncertainty. But I think we stand on our record of improving costs over the last several quarters.

Jim Lucas - *Janney Montgomery Scott - Analyst*

Okay. And you made a comment in your closing remark about working people seeking solutions to real tasks. And specifically one of the areas thats gotten a lot of focus through earnings season was the credit crunch. And whats happened over the last, you know, essentially month. When you look at your industrial markets and you look on both the tools and equipment side, what impact has credit or lack of credit access had on that business and any commentary about near term trends there?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, I think we said -- let me parse between it. We haven't really seen a lot of impact in the industrial business. These are -- generally we're in industries, where these are critical industries that seem to be going forward, and I think I stated that. With the -- order rates have remained strong. So, we feel got about that runway. If you want to expand it to some of the other businesses, I think we said the equipment business, they have some challenges associated with the capital investments in some of their areas. So, they were down, I think, excluding currency 5% in the quarter. And thats directly traceable to this. In the tools business, we see the same kinds of things with big ticket items, big tool storage equipment, big diagnostics. Having said that, though, having said that, the message of the call, I think was, for equipment and for the tool side, innovation is selling. The power tools -- those two power tools, I say, are great tools and they're selling. The Prism new aligner is selling the imaging aligner business is up substantially because of that. Now, some of our other product is off, you might say, even further. But in fact, we believe as we see our new products roll out and we look at our pipeline and feel pretty good about it, it impels purchase even in this difficult time.

Jim Lucas - *Janney Montgomery Scott - Analyst*

Okay. And two final unrelated questions. First, any commentary on tension as you look at that going forward. And secondly with the strengthening dollar, I mean, you've had a nice tail wind on translation for quite some time. What impact do you see FX have going forward?

Marty Ellen - *Snap-on Incorporated - SVP, Finance & CFO*

Jim, it's Marty. First of all, on pension, I can give you the data we have as of the end of September. So, given pension asset values marked-to-market as of September 30 -- and everybody should recall that our funding policy over the past years has pretty much been and our cash flow has allowed us to fund to the PBO level. Our biggest funded plan being in the US. But, given current asset values, but at the same time an increase in the liability discount rate, again looking at that rate at the end of September, all these valuations will have to be re-done at the end of December. But if we just take that point in time, we are still funded -- actually we are modestly overfunded on a PBO basis. Meaning we don't foresee making any pension contributions. Second question on currency rates. I mean, no question the dollar has strengthened. You know, if you look at an example, and I will just pick the euro for example. Last year in the fourth quarter the average rate that drove our P&L was about $1.45. I think yesterday or so, I'm not sure, I'll say $1.32. So, clearly the dollar is strengthening. You can see that across the Pound and the Canadian dollar and the Swedish Krona, which are the more important currencies for us. That being said, when you look at the overall impact of both translation, which by the way added very little to this quarter, you know a few $100,000. But also the transactional exposures that result from us having -- from various of our businesses, the costs base in say Europe and sales in dollars outside Europe or vice versa like in the tools group that makes a lot of product in the US that gets exported into markets in Europe. The effect has been relatively neutral in fact in this quarter when you take translation and transaction, I think the effect on operating income was negative about $1.5 million. Okay? So, the effect of the strengthening dollar? Will it erode reported dollar sales visa vie last year, yes? Not clear to us it's going to have a significant impact given our global model in terms of operating profits.

Jim Lucas - *Janney Montgomery Scott - Analyst*

Okay. Great. Thank you for the clarity.

Operator

All right we'll go to our next question from Alexander Paris of Barrington Research.

Alexander Paris - *Barrington Research - Analyst*

Good morning, nice quarter again.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Thanks Alex.

Alexander Paris - *Barrington Research - Analyst*

You are doing a great job on costs, obviously, and sales is still dragging a bit and I would imagine that even though you've got some good potential ahead for more cost cutting. I'm just wondering where your sales -- you want to get your sales up. It sounds like Eastern Europe and China are your expectations for your biggest source of growth. Is that right?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, no. I would also offer -- thats certainly -- those are two places which are very strong for us. But I think I would argue that -- I would always offer that the whole industrial sector is a big area. You know? We see that -- we're seeing that being pretty strong. So, and thats -- that rides on what we see -- two things, I think, Alex. One is the critical industries that we refer to. Things like aerospace and natural -- oil and gas and natural resources and the like, are continuing to be reasonably robust and theres demand. And secondly, we're gaining share. Because we hadn't -- pretty much the Snap-on brand was trapped in the garage for a long time. So we're rolling it out of the garage and it's capturing the attention of quite a few users. So, we believe pretty clearly that we continue to gain share in that sector. So, you could say the three big drivers -- maybe four big drivers, I'll say. The four big drivers would be, sure the emerging markets, you know, Eastern Europe and Asia Pacific. Two, critical industries and three, and I want to emphasize this, innovation. Because in this market, innovation is still selling. To our customers, innovation is still selling. We saw that with the 2,000 franchisees in August, and we saw a number of activities in this past quarter, the Prism is one of them. I could also add based on an innovation, we haven't really unleashed our diagnostics product in Europe yet. It's been -- the sales there have been relatively small. And over the last quarter we're starting to unlock some of that potential. So, I might add diagnostics and Europe to that play. So, no one -- I want to say, no one can predict where we're going in this volatility. I think you guys read the same articles and see the same papers that we see. No one can predict it. But I can tell you I've been around the block and there's no group of businesses, no group of business models, no brands, no pipeline of products that I'd rather go to war with than the hand we're sitting on right now.

Alexander Paris - *Barrington Research - Analyst*

Part of the strength in the commercial and industrial is you've added more direct sales people to your -- ?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

We have. We added -- in fact, in the quarter, I think -- I don't know the exact number. But I want to say we've added like 25 in the quarter. So, other people are contracting -- we're adding because we believe in that business. Now, that may prove to be wrong, you know. But I think that should emphasize some confidence.

Alexander Paris - *Barrington Research - Analyst*

One other question in the north American dealer, you didn't give account. How many vans do you have at the end of the quarter?

Marty Ellen - *Snap-on Incorporated - SVP, Finance & CFO*

I think the number is what -- ?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Alex at the end of the quarter in round numbers we had about 3450. Its up very slightly, but we think it's a major departure year-over-year from what we've been living with.

Alexander Paris - *Barrington Research - Analyst*

But the territories that you have uncovered, if you were very successful in covering them, what would that add?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

It is about -- I think you would say it's about 10% to the world. Not the world but 10% of that environment. Roughly, 10% of our territories are uncovered. Now, that's come down a little bit because we increased a little bit here. But 10% is a good number.

Alexander Paris - *Barrington Research - Analyst*

So, you could get another 10% of vans without growth overall in terms -- ?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

We think so and I like our positioning versus our competitors in this marketplace to tell you the truth. If you look at the balance between OEM dealerships and independents. Our share is stronger in independents. Our franchisees depend less on OEM dealerships than others. So, if you think, as some people do, I'm not prognosticating, because thats difficult in this environment. If you think that the OEMs are going to reduce by say, 800 or 900 rooftops over a period of time, then I think that shifts in our favor. By the way, over that same period of time, US household spending on auto repairs, it continues to increase. It increased again in August. So, the repairs are going to go someplace. If the OEMs contract, we see the independents ascendent somewhat, we like our positioning in that.

Alexander Paris - *Barrington Research - Analyst*

So, lower new car sales is a negative in terms of warranty work and so forth, but thats probably more than offset by the aging car population.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Sure.

Alexander Paris - *Barrington Research - Analyst*

And more of that goes to the independent dealers than the OEM, right?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

And by the way, if you think about it, the independents -- well, our data tells us this -- the independent dealerships per bay buy more equipment and tools than the OEMs.

Alexander Paris - *Barrington Research - Analyst*

Okay. Just other thing, now that you hit your operating margin of 13% a year earlier, do you have a new target now?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, actually I think it's two years early. I mean it was 2010, but anyway, I have to take full credit for something. No, I don't think -- you know, I think we've talked about targeting in these calls from time to time. But you know, I don't -- I think in this environment, I don't want to get into prediction basis. I think saying that we're going be up in the fourth quarter in earnings is enough for me.

Alexander Paris - *Barrington Research - Analyst*

Okay. Thanks a lot. And again great job.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Okay, thanks.

Operator

(OPERATOR INSTRUCTIONS) We will go next to David Leiker of Robert W. Baird.

David Leiker - *Robert W Baird - Analyst*

Good morning. This is Keith on the line for David. I just have two quick questions here. If we look at the pace of demand as you exited the quarter, a lot of people are talking about Europe slowing meaningfully towards the end of the quarter. I was just wondering if you could talk about the pace of each of the businesses as we exited the quarter.

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, I'll try to give you some overview. Basically on an overview basis we had a pretty strong September, actually. The tools group in the United States had a terrific September, and they were up year-over-year nicely. So, they had a good September. They had a weaker July and August. So, you know in this business, you got a little bit of (inaudible), but anyway, they exited very well. Equipment had a probably, I would say an average September. You know, average to the quarter. They had a September that was about the same. If you look at Europe, they exited weaker than they entered. I'm talking S&A Europe now -- the S&A Europe business exited weaker Asia Pacific and Eastern Europe were both up substantially in September so they continue to go sort of excelsior upward. The diagnostics business had a good September. Diagnostics and information had a good September. So, I think that's it , I think in a broad sense, tools was strong, diagnostics was pretty good, international tools was also strong, the C&I group was mixed. S&A Europe was down. And industrial had a

David Leiker - *Robert W Baird - Analyst*

Perfect. And then if we look to the fourth quarter, with the year-over-year increase in earnings, is this going to be driven more by revenue growth with whats coming, the normalization, the C&I business or is this more of a margins story in the fourth quarter?

Nick Pinchuk - *Snap-on Incorporated - President and CEO*

Well, I don't think I really want to, you know, specify between that. I mean our history is that we've been able to make -- as I said I think in my remarks, I think we have confidence in our ability to balance between sales growth and cost reduction. So, we feel pretty good about the cost reductions we see going forward. If we get some revenue growth that will be nice as well. But, I think it's very difficult predict the way in which such a thing might eventuate in this environment, so I don't think I will.

David Leiker - *Robert W Baird - Analyst*

Okay, thank you very much.

Operator

And it appears we have no further questions on the phone at this time. I'd like to turn the call back over to Marty Ellen for any additional or closing remarks.

Marty Ellen - *Snap-on Incorporated - SVP, Finance & CFO*

Thank you again everyone for joining us this morning. We appreciate your interest in Snap-on. Good day.

Operator

And again, ladies and gentlemen, we thank you for your participation. You may disconnect at this time.
