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HEADLINE: Is There a Screw Loose at Snap-on?;
The company has a killer business and a storied brand name, but CEO Robert Cornog seems to be missing some key tools.

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BODY:

To the mechanics who earn their living beneath the greasy undercarriages of imported luxury cars at Lorenzutti Motors in Brooklyn, New York, Tuesday afternoon is sacred. That's when Brian the Snap-on Man drops by.

Brian McAlister is a soft-spoken 34-year-old with shaggy blond hair and a goatee. He's a dealer for Snap-on, the Wisconsin tool manufacturer legendary among mechanics for the quality of its products and among marketing experts for the genius of its sales methods. The last of the great American door-to-door sales forces, McAlister and the 6,000 other Snap-on dealers drive from garage to garage, their distinctive white trucks serving as mobile showrooms. When McAlister arrives at Lorenzutti on a Tuesday in June, four mechanics pile into the back of his van like kids into a toy store. Manuel Juca buys a $ 59 torque gauge; Isidro Valle adds a $ 49 chain wrench to his collection, and so on. In the space of half an hour, McAlister has sold $ 500 worth of tools.

Back at Snap-on headquarters in Kenosha, Wis., however, success has been harder to come by. A slew of misguided acquisitions, a disastrous enterprise-software installation, and a litany of other executive fumbles have infuriated investors--and for good reason. The stock's total return over the past five years is just 17%, a depressing 174 percentage points behind the S&P 500. Snap-on, for all its savvy marketing, is fast becoming a study in the tarnishing of a great American brand.

The easy assumption is that Snap-on's problems stem from its old-economy business model. Selling door to door might have been cutting-edge when young tool-works manager Joseph Johnson founded Snap-on in 1920 (the company was named for its interchangeable wrench heads, which snapped onto a variety of handles), but today it seems hopelessly quaint. Avon, Mary Kay, World Book, and other companies that relied on pavement-pounding salespeople have either gone out of business or drastically changed their style.

Snap-on, however, is a different story. "I love the Snap-on tools," says Juca as he proudly shows off the contents of his red Snap-on tool chest. Snap-on's products aren't cheap--in fact, they can cost several times as much as competing brands--but independent mechanics (who often spend $ 30,000 over a career on tools) say the quality is worth it.

When a customer can't pay for a tool on the spot, McAlister--adhering to a practice Snap-on pioneered during the Great Depression--lets him pay in weekly installments of $ 20 to $ 60. For less expensive items, Snap-on extends this credit interest-free, and most mechanics barely notice the mounting account balance. They simply hand over a couple of crumpled-up bills each week and buy a few more tools. McAlister, on the other hand, knows exactly how much each of the 200 to 300 mechanics on his

route has spent. He tracks it all on a laptop computer in his van. "They owe me forever, but I try not to overextend them on credit," he says.

This formula--peerless quality and easy credit--has created a surprisingly large and vibrant market. The average Snap-on dealer sells about $ 350,000 worth of tools a year, making his 160 square feet of van among the most productive retail spaces in the world. The company owns a staggering 60% share of the market for professional automotive tools. (Its nearest competitor, the Mac tools subsidiary of Stanley, has just 13%.) Thanks to the growing complexity of cars and the quickening pace of new-model introductions--the 2001 version may require a whole other set of tools than the 2000 model--the market is growing reliably, if deliberately, at 5% a year. To make sure the dealers capture all that growth, the company is introducing a highly regarded Net strategy that makes Snap-on products available to online customers 24 hours a day.

So don't blame Snap-on's problems on its line of business. If you want to find the monkey wrench in the works, say a growing number of analysts, former employees, and investors, look for it in the corner office occupied by 60-year-old CEO Robert Cornog. At the company's annual meeting in April, a parade of shareholders angrily questioned Cornog's leadership. Many were incensed that his compensation totaled $ 2.1 million last year, up 159% from 1998, even though the stock's total return in 1999 was -22%. Cornog was unapologetic, declaring that his salary was comparable with that of other CEOs and had been determined by a formula the shareholders themselves approved.

Several major stockholders have complained directly to members of Snap-on's board of directors. One was the company's second-largest institutional investor, New York investment firm First Manhattan, which holds about 6.4% of Snap-on's stock. Among the others were the heirs of company founder Johnson, who are among Snap-on's largest individual shareholders. "In the best interests of the company," says Mary Johnson, the founder's daughter-in-law, "we would like to see some changes in leadership." So far the board has listened to shareholder complaints but announced no action. "We are working on what we are going to do differently," says George Mead, one of Snap-on's directors and the chairman of Consolidated Paper.

Since Cornog arrived at Snap-on from steel cable manufacturer MacWhyte in 1991, the linchpin of his strategy has been acquisition. By late last year he had bought 25 companies, spending some $ 800 million in cash and stock. A few have worked out--like Snap-on's 1991 purchase of Balco, a manufacturer of wheel-service equipment and handheld electronic diagnostic devices, and its 1992 takeover of Sun Electric, a high-end diagnostics company. Both helped Snap-on adapt to the new reality of computerized cars, and today a third of the products Snap-on sells have a software component.

But many of Snap-on's other purchases have been duds. In 1998, Snap-on wrote off $ 36.5 million in goodwill from its purchases of Computer Aided Services and Edge Diagnostics, both of which it had acquired in the previous three years. Last year it wrote off another $ 16.9 million from an ill-fated move into emissions-testing equipment. Normally an acquirer has to amortize goodwill over decades, so to write it off all at once, as Snap-on did, means trouble. "It's a clear admission of a mistake," says a money manager who sold his Snap-on shares in disgust last year. (Cornog blames the write-offs on unforeseeable shifts in technology.)

The company's seven European acquisitions have so far done little to improve either its market share or its returns overseas. According to First Manhattan, Snap-on has about $ 900 million in capital invested in the U.S., on which it earns an 18% return. It has another $ 900 million invested in Europe but earns only 6% on that money. One institutional money manager quips that Snap-on's only European strategy is "to keep throwing good money after bad." In its 1998 SEC filings, the company acknowledged that several of its European acquisitions had "lower-than-expected performance." After that, the company ceased breaking out its profits and revenues by geographic segment.

In September, Snap-on bought Sandvik Saws & Tools, a Swedish producer of high-end woodworking and landscaping tools, for $ 380 million in cash--its most expensive acquisition to date. Sandvik, which Snap-on renamed Bahco, has a strong presence in Europe, but some analysts and dealers (who complain of

back orders on standard automotive tools) consider it a mismatch with the U.S. business. "They can't get me a 9/16-inch socket wrench, but they send us pruning shears and brush saws from Sandvik," grouses Dave Peters, a Boston-area dealer. Peters says he eventually offloaded his shears and saws, but grumbles, "That's not the business I'm in." Cornog says the Sandvik tools were intended as Father's Day and Mother's Day promotions and that they sold well.

Snap-on has also irked some investors by its choice of acquisition targets. "They've bought a lot of old iron," says Willy Borner, a co-founder of Balco who continued to work for Snap-on until 1996. Borner and former Balco partner Bernie Jackson, who each control about 250,000 shares, are among those who have complained to the company's board. The two would have liked to see Snap-on move more aggressively into computerized diagnostics. Instead, Jackson says, the company bought mechanical-tool businesses that competed with its existing products. "With large overlaps, you don't get the value of what you are acquiring," he says.

The company all but conceded this point when it announced a $ 187 million restructuring plan dubbed Project Simplify in 1998. The restructuring, which was completed earlier this year and which Snap-on says will save it $ 60 million annually, discontinued dozens of products. It closed six plants, seven warehouses, and 47 offices and eliminated 1,100 jobs, 9% of the company's work force.

To some, the restructuring is a clear indication that management is clueless. "You don't just suddenly run up against a wall and have to write off $ 180 million," says Ken Ragan, Snap-on's vice president of international sales until he retired ten years ago. "These problems have been going on since they started buying this stuff." Cornog defends Project Simplify, saying, "Snap-on believes the use of Simplify for cost reduction was better accepted throughout the organization and in the marketplace than cutting off the tail of the dog one inch at a time."

In any event, Snap-on could hardly have chosen a worse moment to undertake a massive restructuring. In 1998 the company was installing a new $ 54 million back-office computer system, and things were going badly--very badly. The new system reduced the company's purchasing and inventory management to chaos for more than a year. As back orders multiplied, operating income from U.S. van sales plummeted 51%. Some of Snap-on's own dealers resorted to buying tools and equipment from other suppliers. The company spent heavily on overtime and shipping charges, and productivity plunged. Combined with Snap-on's restructuring, the computer problems resulted in a $ 4.7 million loss in 1998, the first in Snap-on's history. Profits have since recovered to $ 127 million but remain 15% below their 1997 levels.

Granted, Snap-on is hardly the first corporation to botch a major computer installation. In Snap-on's case, however, the problems speak to wider management deficiencies. "Snap-on was not experienced enough to pick up the slack or even realize that someone else had taken their eye off the ball," concludes Bruce Bond, group vice president for enterprise and supply-chain management at the Gartner Group. It was Gartner that Snap-on contacted for advice after its installation ran into trouble. Snap-on says its back-office system, made by Dutch software company Baan, is now working well.

Cornog's critics also cite Snap-on's inability to communicate effectively with Wall Street. Cornog badly bruised his credibility on the Street when he announced the restructuring and resulting net loss just three months after an analysts' conference in which he and CFO Donald Huml repeatedly waxed optimistic over the company's growth outlook. "They promised Wall Street one thing and then cut it off at the knees," says shareholder Jackson. "The investment community won't forgive that anytime soon."

The company further hurt its standing with shareholders when it created an unusual stock trust in the summer of 1998. The trust, which Snap-on called a Grantor Stock Ownership Plan, appears similar to those instituted by Disney and Ralston Purina, among others. The trusts, designed to fund employee-benefit plans, may help improve a company's bond rating. In Snap-on's case, the trust got 7.1 million shares, or 11% of all shares outstanding, in exchange for a $ 260 million IOU.

But Snap-on's trust differed from others in one crucial regard: voting rights. The trust allowed company executives to vote their shares based on the number of options they held. That meant managers could vote stock they did not even own, effectively diluting other shareholders' voting rights. In one instance, a senior vice president who had only 25,000 shares could have voted 500,000 shares based on his options.

Cornog claims Snap-on's trust was intended to increase shareholder value. But others believe its real purpose was to serve as a takeover defense by giving management a disproportionately large vote. The critics also ask why, if Snap-on's trust was so shareholder-friendly, the company didn't tell shareholders about it? First Manhattan, the second-biggest owner of Snap-on stock, discovered the trust only by chance during a routine perusal of Snap-on's SEC filings. The investment firm passed the information on to the other nine largest shareholders--the first that many of them had heard of it. For most, it was the last straw: They bailed out of Snap-on stock, contributing further to its decline. Although the company eventually softened the controversial voting provision, only Fidelity and First Manhattan today hold more than 5% of the company's shares.

Snap-on has also managed to alienate another key constituency--its sales force. The dealers, most of whom are independent franchisees, still account for 60% of sales and operating income, but many fear the company is taking them for granted--or worse, milking them for profit. One sore point: Project Simplify eliminated 150 of the dealer supervisors known as field managers. As a result, field managers who once oversaw six to nine dealers now handle up to 15. "You can't service that many people in the way they were accustomed to be serviced," says Evan Sermos, a former Massachusetts field manager. Sermos and others also fret about a reduction in the size of territories granted new dealers--from an average of about 270 mechanics three years ago to about 220 today. (The company says it never promised more than 200 mechanics.) Sermos, a 16-year veteran whose team was frequently among the top sellers in the Northeast, resigned last month over what he felt was improper treatment of dealers.

Clark Heintz, a New Hampshire dealer and a member of Snap-on's national dealer advisory council--a group of 16 franchisees that represents the whole group in meetings with management--blames the dealers' declining morale on poor communication. "The dealers form their own opinions through a lack of information," says Heintz. But Cornog himself has passed up several opportunities to dispel confusion. Although he travels on all the congratulatory junkets for top salesmen (the most recent was to the Caribbean in March), he has never made a speech to them. Cornog says he doesn't feel it's his job. Instead, he attends every advisory council meeting and says he frequently meets one-on-one with other dealers.

To investors worried about Snap-on's future, perhaps the company's most glaring problem is its lack of executive depth and a clear succession plan. When a ruptured colon sidelined Cornog for four months earlier this year, CFO Huml handled day-to-day operations. But shareholders complain that Huml, who has practically no operating experience, is unfit to be CEO. Board member Mead says that a succession plan is "one of the things we're working on."

Some investors and analysts would like to see the board work on selling the company instead. "That would improve shareholder value in a heartbeat," says Lehman analyst Darren Kimball. One possible buyer popular with some shareholders is Illinois Tool Works, whose president, Frank Ptak, just joined Snap-on's board.

Others believe a sale is unnecessary. They claim Snap-on's problems are in the past. The company just needs to consistently meet earnings expectations and its stock will soar. But that's what a lot of the same analysts were saying four years ago. Since then Snap-on's stock has gone nowhere. And until the company's board tightens Snap-on's loose screws, perhaps it never will.

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GRAPHIC: TWO B/W PHOTOS: PHOTOGRAPHS BY ALEX TEHRANI, Tools of Snap-on's trade: a die (above) for threading bolts; an impact driver (right); B/W PHOTO: PHOTOGRAPHS BY ALEX TEHRANI, Snap-on tools can cost far more than competing brands, but mechanics say they're worth it.; B/W PHOTO: PHOTOGRAPHS BY ALEX TEHRANI, McAlister's van is wildly efficient retail space. Typical sales per square foot: $ 2,200; COLOR CHART: FORTUNE CHART, Time for a Tune-Up S&P 500, Snap-on; B/W PHOTO: PHOTOGRAPHS BY ALEX TEHRANI, Manuel Juca and Otto Aldana (in company colors) wield a Snap-on welder at Lorenzutti Motors.

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