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ACQUIRING MIND

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BY BOB TITA

David Speer unwittingly hitched his wagon to James Farrell's star in 1978. Mr. Farrell, then head of Illinois Tool Works Inc.'s construction-products group, hired Mr. Speer to sell hardware. As Mr. Farrell rose through ITW, he brought Mr. Speer along, making him a general manager at the age of 33. After Mr. Farrell became CEO in 1995, he made Mr. Speer an executive vice-president and, nine years later, promoted him to president.

"He put me through a number of different assignments," Mr. Speer says. "I think he did that for a purpose."

The purpose became clear when Mr. Farrell designated Mr. Speer his successor as CEO. But for all Mr. Farrell bequeathed him, Mr. Speer, 55, who took over the top spot in 2005, is now left with the unenviable task of contending with his mentor's legacy.

In his decade as CEO, Mr. Farrell made ITW, a seemingly mundane industrial conglomerate, into a Wall Street rock star, posting average annual earnings growth of 14%. Mr. Farrell cemented ITW's reputation as a shrewd acquisition machine that bought profitable manufacturers and made them more profitable, while allowing the acquired companies' management to operate in near-complete autonomy. At the end of 2006, ITW had about 750 different businesses.

Maintaining that exalted status will require Mr. Speer to take Glenview-based ITW into uncharted territory. Since Mr. Speer took over, two of ITW's biggest business lines—construction and auto parts, which account for about 25% of the company's $13 billion in annual sales—have hit the skids, thanks to steep downturns in homebuilding and U.S. auto production. ITW lowered its earnings forecasts twice in the second half of 2006. And after a stellar run-up in recent years, ITW's stock finished 2006 with a market-trailing 5% gain.

"We're entering a period where the (earnings) numbers are going to be reduced," says Eli Lustgarten, an analyst with Ohio-based Longbow Research. "The revenue growth for 2007 is becoming somewhat more suspect."

A SALESMAN'S CHARM

The third of seven children who grew up moving from town to town following their father's career in the chemical industry, Mr. Speer graduated from high school in suburban Barrington, then earned an engineering degree from Iowa State University—but only because he wanted to sell technical products. When he interviewed with Mr. Farrell, Mr. Speer was selling electrical insulation and had just earned a night-school MBA from Northwestern University.

Mr. Speer says he has always seen himself as a salesman. Lately he's been plying all of his salesman's charm and polish to convince Wall Street he can keep ITW growing at the rate investors expect. He boldly predicts 10% to 13% sales growth and 12%

to 15% profit increases for the next five years. To deliver, he'll have to continue last year's frantic pace of acquisitions—and he'll have to export the vaunted ITW business model to the far side of the world, where it will face unprecedented obstacles.

RECORD-BREAKING DEALS

Last year, Mr. Speer outdid Mr. Farrell and all previous ITW bosses with a record 53 acquisitions, adding $1.7 billion in revenue.

Nearly all of those deals were done without investment bankers or Mr. Speer's direct involvement. In fact, he says, he couldn't name more than three-quarters of the companies ITW bought in 2006. To Mr. Speer, that's proof that one of his signature initiatives is working.

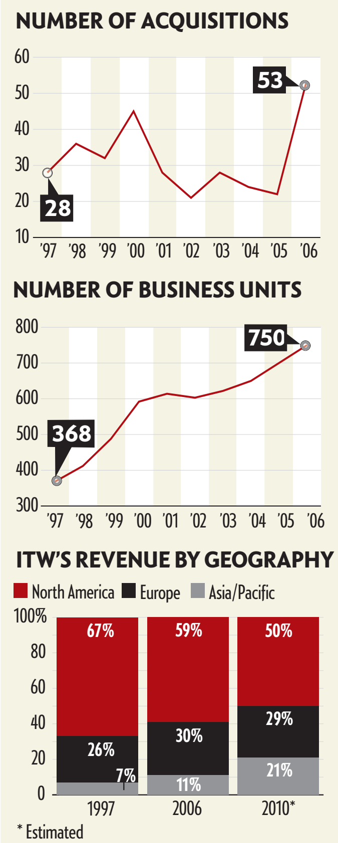
Shortly after taking over as CEO, Mr. Speer saw the need to do more deals and knew he'd need more help from the managers of the company's business units.

"We recognized that we had only some of the businesses actively involved in acquisitions," he says. "We had a lot of young managers who were not active."

So, in the past 16 months, ITW has put 150 managers through in-house training to sharpen their skills at spotting good acquisition targets and putting deals together. The managers are taught to look for companies that meet ITW's 80/20 standard: That is, they get 80% of their sales from 20% of their customers. The managers also learn that when newly acquired companies don't meet profitability targets, they and they alone will be responsible for fixing them. That accountability is what allows Mr. Speer to pilot ITW without keeping tabs on all of the business units it accumulates.

"When people ask me, 'How do you run 750 companies?' I tell them I don't," he says.

ITW'S GROWTH SPURT



* Estimated

Source: Illinois Tool Works

'WE NEED CHINESE MANAGERS'

But as well as ITW's decentralized culture has served it in the past, the model has been slow to take hold in Asia. The problem: a shortage of small and medium-sized companies that fit ITW's acquisition criteria and a scarcity of native managers capable of executing the 80/20 strategy.

"It's taken us longer because of our business model," Mr. Speer admits.

Since Chinese executives have proved hard to find, Mr. Speer has chosen to grow them himself using a new tactic for ITW: building factories rather than buying them, then staffing the plants with Chinese managers recruited and trained by the company. Mr. Speer is counting on this corps of managers to start reeling in acquisitions of existing Chinese businesses, just like their counterparts in the U.S.

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ITW encompasses 750 units, including Signode industrial packaging in Glenview, above.

He can't afford for the tactic to fail. Mr. Speer has forecast that total Asia-Pacific revenue will reach $4 billion a year by 2010—up from $1.7 billion last year.

Some wonder whether that outlook isn't a bit optimistic, given the pace of the company's penetration into Asia so far.

"I would call it a stretch goal," says analyst Matthew Collins of Edward Jones in St. Louis. "You're still going to have to be successful at finding acquisitions."

And that will depend on Mr. Speer and his team's ability to find the right managers. That's always been the case at ITW; just ask Mr. Farrell, the former CEO who took a chance on a young insulation salesman 29 years ago.

"You just can't afford not to trust people," Mr. Farrell says. "As you get older and as you succeed, you always remember the people you had success with down in the ranks."

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