

## Fastener Distributor Index – March 2019

Written by R.W. Baird analyst David J. Manthey, CFA 4/5/19



**Key Takeaway:**

The seasonally-adjusted FDI for March was 53.0, relatively stable with February’s 52.5 and consistent with an essentially unchanged reading in last month’s FLI. Sales trends were slightly weaker for the second consecutive month with the seasonally-adjusted sales index now below 50. Respondent commentary was also cautious with several survey participants noting growth has softened. The six-month outlook was stable, but the Forward-Looking Indicator slipped further into contractionary territory.

**Fastener Distribution Trends: March 2019**

<b>FASTENER DISTRIBUTION AT A GLANCE</b>										
<b>March 2019</b>										
	----- Index Values -----								Directbn	Rate of Change
	Mar	Feb	Jan	Dec	Nov	Oct	Sep	Aug		
PMI (Manufacturing Sector)	55.3	54.2	56.6	54.1	59.3	57.7	59.8	61.3	Growing	Faster
FDI (Fastener Sector)	54.4	50.9	60.2	55.6	56.9	62.0	52.8	61.7	Growing	Faster
<b>FDI (Seasonally Adjusted)</b>	<b>53.0</b>	<b>52.5</b>	<b>56.5</b>	<b>56.5</b>	<b>58.2</b>	<b>62.2</b>	<b>55.8</b>	<b>62.5</b>	Growing	Faster
Sales (SA)	45.3	51.3	62.2	58.1	51.8	73.4	46.5	74.7	Declining	Faster
Forward- Looking (SA)	46.9	49.6	49.8	54.1	52.5	57.0	54.7	63.4	Declining	Faster
<b>{Other Metrics; NSA}</b>										
Employment	56.5	51.7	57.4	66.1	64.5	67.3	61.1	67.2	Growing	Faster
Supplier Deliveries	62.9	62.1	61.1	59.7	69.7	61.5	63.0	70.3	Growing	Faster
Respondent Inventories	72.6	60.3	70.4	62.9	64.5	57.7	59.3	59.4	Growing	Faster
Customer Inventories	48.4	43.1	44.4	43.5	47.4	40.4	46.3	32.8	Declining	Slower
Pricing, month-to-month	67.7	62.1	59.3	71.0	76.3	75.0	70.4	76.6	Growing	Faster
Pricing, year-to-year	85.5	81.0	83.3	91.9	90.8	88.5	92.6	92.2	Growing	Faster
6-Month Outlook - March					Higher	Same	Lower			
					32%	45%	23%			

*FDI and Pricing are diffusion indexes. At 50, the performance of the category listed met expectations. A reading above 50 suggests the category outperformed expectations, while a reading below 50 suggests the category underperformed expectations.*

Source: Baird, FCH Sourcing Network, Institute for Supply Management

**About the Fastener Distributor Index (FDI).** The FDI is a monthly survey of North American fastener distributors, conducted with the **FCH Sourcing Network**, the **National Fastener Distributors Association**, and **Baird**. It offers insights into current fastener industry trends/outlooks. Similarly, the Forward-Looking Indicator (FLI) is based on a weighted average of four forward-looking inputs from the FDI survey. This indicator is designed to provide directional perspective on future expectations for fastener market conditions. As diffusion indexes, values above 50.0 signal strength, while readings below 50.0 signal weakness. Over time, results should be directly relevant to **Fastenal (FAST)** and broadly relevant to other industrial distributors such as **W.W. Grainger (GWW)** and **MSC Industrial (MSM)**.

**Key Points:**

**FDI stable in March.** The seasonally-adjusted March FDI (53.0) was stable vs. February (52.5), consistent with an unchanged reading in the FLI last month. The sales index decelerated and slipped below 50 for the first time in five months, as only 32% of respondents saw higher than seasonally expected sales in March (2018 average was 55%). Positively, pricing was slightly improved m/m. Customer inventory levels continue to be perceived as in line with expectations, while respondents' inventories were more elevated than typical for the second month out of the past three.

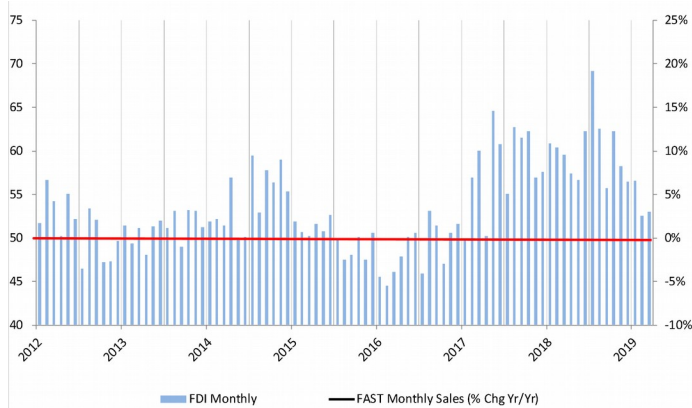
**March FLI dips further into contractionary territory.** The seasonally-adjusted FLI weakened further vs. February to 46.9 (vs. 49.6 last month) and remained below 50 for the third straight month. Of the four FLI components (employment index, respondent inventories, customer inventories, and 6-month outlook), all but the employment index weakened sequentially. Looking back to the most recent time the FLI had three consecutive sub-50 readings (March-May 2016), the subsequent four FDI readings were all near or below a neutral level of 50. In light of this, we continue to believe stabilization or further moderation in the FDI is likely.

**Hiring sentiment improves.** Hiring sentiment improved this month as hiring was in line to above seasonal expectations for more fastener distributors when compared with February. The resulting FDI Employment Index improved by ~5 points sequentially. On an economy-wide basis, the March US jobs report rebounded from a much weaker February report with a better-than-expected 196,000 jobs added (~175,000 expected). The unemployment rate held steady at 3.8%. March's largest gains were registered in health care and in professional and technical services. Manufacturing employment declined slightly (-6,000 m/m), a notable change from the average of 22,000 jobs added per month prior to last month's modest gains (+1,000) and this month's slight decline. Average hours per work week for manufacturing employees was unchanged at 40.7 hours.

**Respondent commentary remains cautious.** Qualitative commentary was again cautious overall as several respondents noted continued softening in market conditions. One respondent summarized the environment stating, "Starting to see signs of slowdown... I foresee a slowdown and slower growth in 3rd or 4th quarter to level off." Unfavorable weather conditions likely also negatively impacted results, as one participant noted "My customers say they have a lot of jobs booked but on hold due to rain. I think it will get super busy in the next couple of months. Shortage of people however here in northern CA will be an issue." The six-month outlook mostly points to stable activity levels anticipated by fastener distributors over the next six months, with 32% of respondents expecting higher activity levels, 45% expecting similar activity, and 23% expecting lower activity. For context, the percentage of respondents expecting higher activity throughout 2018 was 49% on average, while the percentage expecting lower activity was 14%.

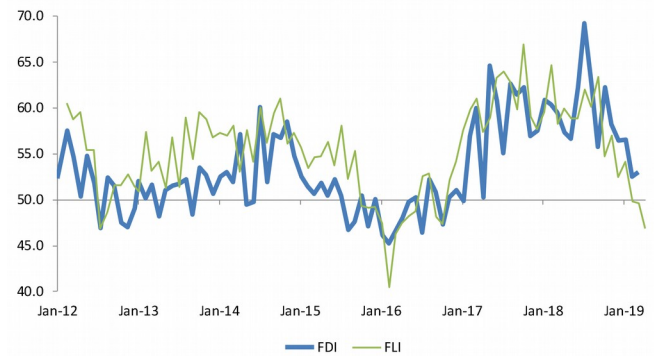
**Fastenal** reported 10.5% February daily sales growth, which was consistent with our +10.4% estimate. Underlying organic growth of +11.0% matched our estimate despite a 1.3%-1.6% weather headwind, and was the 21<sup>st</sup> straight month of double-digit growth. Consistent with the deceleration seen in the February FDI and January's weak FLI reading, fastener growth decelerated m/m to +8.7% y/y (+13.3% in January). Based on FDI data and other research inputs, we largely expect still-solid, but potentially moderating, top-line trends across public industrial distributors in 2019, partially offset by higher pricing. Fastenal's March daily sales growth will be reported with quarterly earnings on April 11.

## Fastener Distributor Index (FDI); Seasonally Adjusted



Source: Baird, FCH Sourcing Network, Company reports

## 1-Month Lagged FDI vs. FLI (Both Seasonally Adjusted)



Source: Baird, FCH Sourcing Network

## Risk Synopsis

Fastenal: Risks include economic sensitivity, pricing power, relatively high valuation, secular gross margin pressures, success of vending and on-site initiatives, and ability to sustain historical growth.

Industrial Distribution: Risks include economic sensitivity, pricing power, online pressure/competitive threats, global sourcing, and exposure to durable goods manufacturing.

## Appendix – Important Disclosures and Analyst Certification

### Covered Companies Mentioned

All stock prices below are as of 4/5/2019.

Fastenal Company (FAST-\$66.53-Neutral)  
 W.W. Grainger Inc. (GWW-\$316.05-Neutral)  
 MSC Industrial Direct Co. Inc (MSM-\$85.20-Neutral)  
 (See recent research reports for more information)



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