

Fastener Distributor Index – January 2020

Written by R.W. Baird analyst David J. Manthey, CFA 2/5/20



Key Takeaway:

The seasonally adjusted Fastener Distributor Index (FDI) for January was **51.4**, accelerating nicely vs. December and returning to growth territory. Sales trends on a seasonally adjusted basis were much improved m/m, with a slight majority of respondents' sales coming in above expectations. The six-month outlook and the Forward-Looking Indicator (FLI) also both improved sequentially, with the FLI returning to expansionary territory for the first time since early 2019. Overall, fastener market conditions started off the year on a solid note in January, while respondents' implied February forecasts are for continued moderate improvement given an FLI slightly above 50.

Fastener Distribution Trends: January 2020

FASTENER DISTRIBUTION AT A GLANCE										
January 2020										
	----- Index Values -----								Direction	Rate of Change
	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun		
PMI (Manufacturing Sector)	50.9	47.8	48.1	48.3	47.8	49.1	51.2	51.7	Growing	Faster
FDI (Fastener Sector)	55.4	43.4	45.5	52.2	52.4	55.5	50.9	48.8	Growing	Faster
FDI (Seasonally Adjusted)	51.4	44.4	46.7	52.1	56.0	55.9	52.2	48.3	Growing	Faster
Sales (SA)	50.0	34.9	35.5	48.2	56.4	52.1	40.4	38.5	Growing	Faster
Forward- Looking (SA)	50.9	46.2	46.5	44.2	44.0	48.0	44.9	44.4	Growing	Faster
(Other Metrics; NSA)										
Employment	56.7	45.3	48.5	48.7	51.6	55.9	55.4	56.5	Growing	Faster
Supplier Deliveries	58.3	53.1	51.5	55.1	58.1	58.8	64.3	50.0	Growing	Faster
Respondent Inventories	63.3	65.6	65.2	69.2	69.4	64.7	69.6	61.3	Growing	Slower
Customer Inventories	41.7	43.8	51.5	52.6	53.2	52.9	48.2	51.6	Declining	Faster
Pricing, month-to-month	58.3	60.9	57.6	59.0	61.3	61.8	66.1	66.1	Growing	Slower
Pricing, year-to-year	70.0	79.7	78.8	84.6	79.0	80.9	80.4	82.3	Growing	Slower
Higher Same Lower										
6-Month Outlook -January				33%	50%	17%				

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** and **Baird** with support from the **NFDA**. 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 surges back above 50. The seasonally adjusted January FDI (51.4) surged from a lackluster December reading (44.4), returning to growth. This was driven by much stronger selling conditions, which produced a seasonally adjusted sales index of 50.0 vs. just 34.9 last month, as well as improvement in the survey's employment component. After two consecutive months of sales falling short of expectations for a majority of respondents, the trend reversed this month, with 53% of respondents seeing sales growth above seasonal expectations, while just 23% characterized sales as below seasonal expectations. Lastly, pricing remained stable sequentially for a large majority of respondents.

January FLI also improves m/m, also now back above 50. The seasonally adjusted FLI accelerated to 50.9 (December 46.2), reflecting improvements among all four components (six-month outlook, respondent inventories, customer inventory levels, and employment). While coming in only moderately above 50, this represented the first expansionary FLI reading since April 2019, implying near term demand conditions could remain stable or improve slightly further in February.

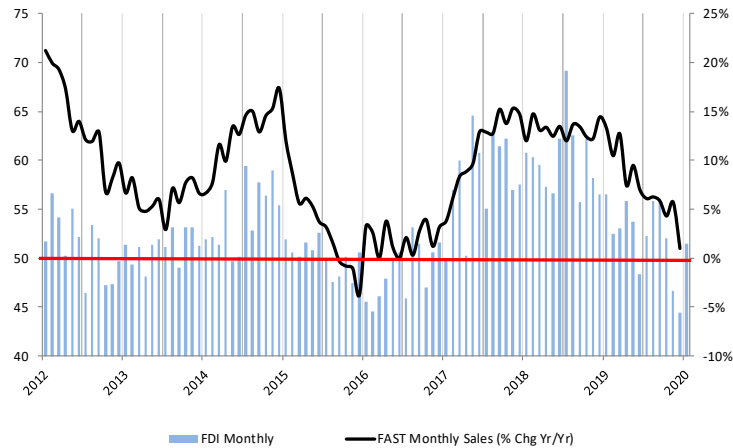
Hiring sentiment improves. Sentiment around hiring was slightly more optimistic m/m, as 27% of respondents characterized the pace of hiring as having picked up vs. December, while another 60% indicated the pace was stable sequentially. Looking at the broader economy, the December jobs report was moderately weaker than anticipated with 145,000 job additions vs. economist expectations of +160,000. This continues the recent trend of positive but moderating gains, as the rate of adds has slowed since the end of 2018, when the economy was adding an average of 223,000 jobs per month. The unemployment rate was stable at 3.5%. Manufacturing employment in December declined moderately m/m with a decrease of 12,000 jobs. The January jobs report is slated to be released on February 7 where economists forecast 160,000 job additions.

Respondent commentary still skews negative. While trends were on balance better than expected for a majority of respondents in January, qualitative feedback still suggested a fairly muted demand environment. One respondent commented, "Starting the year [with a] flat month for January." Another commented, "Auto sector is trending lower." The six-month outlook did show improvement, however, with only 17% of respondents now expecting lower activity six months from now (down vs December 28%), 50% expecting similar activity (December 47%), and 33% expecting higher activity (December 25%).

FCH Sourcing Network website inventory search volume increased to over 121,000 on a daily average of 1.56 million parts listed by FCH members during the month.

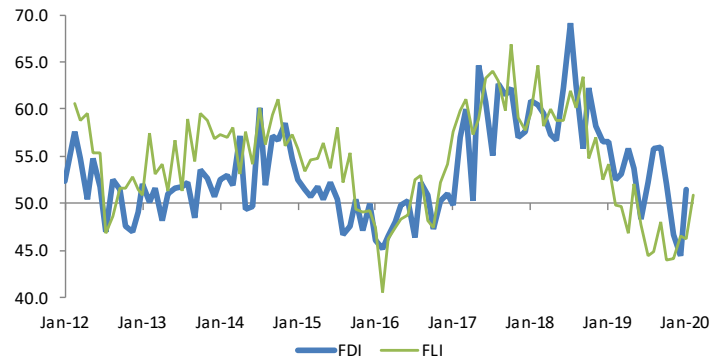
Fastenal reported +1.0% overall December daily sales growth, well below our +3.2% estimate. Sales growth to manufacturing customers decelerated nearly 6% m/m, while non-residential construction end market growth decelerated ~5% sequentially. Overall organic growth of +0.9% moderated significantly vs. +5.8% in November. Fastener sales specifically fared slightly worse with sales decreasing 0.5% y/y (November +2.4%), consistent with the weaker FDI reading last month. January daily sales growth will be reported on February 6. Based on FDI data and other research inputs, we somewhat conservatively model January ADS +1.7%, slightly below normal seasonal trends would imply given mixed January signals from other publications, and private distributors and industrial indicators.

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.

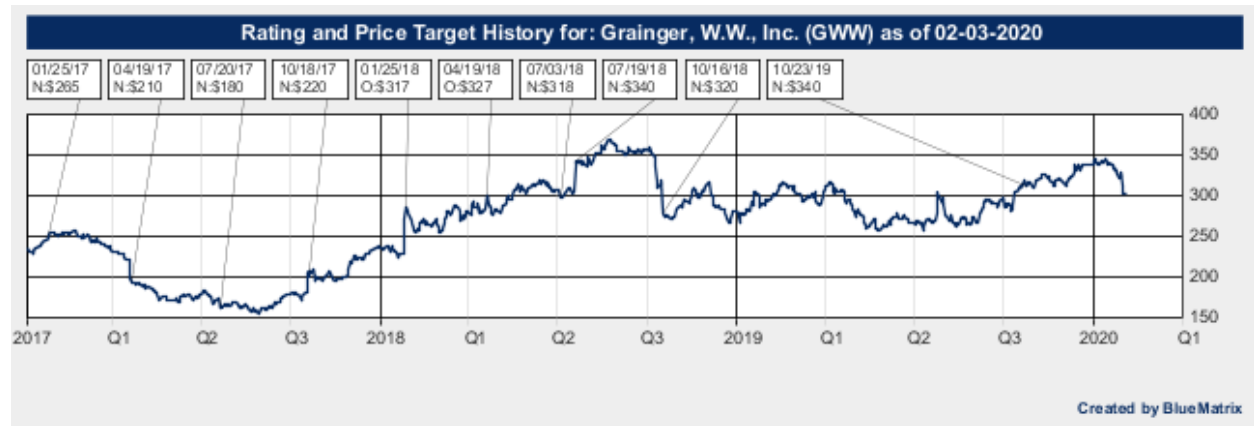
Industrial Distribution: Risks include economic sensitivity, pricing power, online pressure/competitive threats, global sourcing, and exposure to durable goods manufacturing.

Appendix – Important Disclosures and Analyst Certification

Covered Companies Mentioned

All stock prices below are as of 2/4/2020.

Fastenal Company (FAST-\$36.93-Neutral)
 W.W. Grainger Inc. (GWW-\$308.14-Neutral)
 MSC Industrial Direct Co. Inc (MSM-\$70.73-Neutral)
 (See recent research reports for more information)



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