

Fastener Distributor Index – May 2019

Written by R.W. Baird analyst David J. Manthey, CFA 6/6/19



Key Takeaway:

The seasonally-adjusted Fastener Distributor Index (FDI) for **May** was **53.8**, contracting two points vs. April's 55.8 reading. Sales trends mirrored the overall index, as the seasonally-adjusted sales index also moderately retreated from April levels. Respondent commentary similarly remained cautious on balance, as both the six-month outlook and the Forward-Looking Indicator (FLI) reverted lower m/m. The FLI specifically returned to sub-50 levels for the fourth time YTD. Overall, results were less encouraging in May than in April.

Fastener Distribution Trends: May 2019

FASTENER DISTRIBUTION AT A GLANCE										
May 2019										
	Index Values								Direction	Rate of Change
	May	Apr	Mar	Feb	Jan	Dec	Nov	Oct		
P/M (Manufacturing Sector)	52.1	52.8	55.3	54.2	56.6	54.1	59.3	57.7	Growing	Slower
FDI (Fastener Sector)	55.9	57.8	54.4	50.9	60.2	55.6	56.9	62.0	Growing	Slower
FDI (Seasonally Adjusted)	53.8	55.8	53.0	52.5	56.5	56.5	58.2	62.2	Growing	Slower
Sales (SA)	57.4	61.3	45.3	51.3	62.2	58.1	51.8	73.4	Growing	Slower
Forward-Looking (SA)	47.7	52.1	46.9	49.6	49.8	54.1	52.5	57.0	Dedining	Faster
[Other Metrics; NSA]										
Employment	57.8	55.4	56.5	51.7	57.4	66.1	64.5	67.3	Growing	Faster
Supplier Deliveries	60.9	66.2	62.9	62.1	61.1	59.7	69.7	61.5	Growing	Slower
Respondent Inventories	65.6	66.2	72.6	60.3	70.4	62.9	64.5	57.7	Growing	Slower
Customer Inventories	43.8	41.9	48.4	43.1	44.4	43.5	47.4	40.4	Dedining	Slower
Pricing, month-to-month	62.5	58.1	67.7	62.1	59.3	71.0	76.3	75.0	Growing	Faster
Pricing, year-to-year	89.1	82.4	85.5	81.0	83.3	91.9	90.8	88.5	Growing	Faster
6-Month Outlook - May				Higher			Same		Lower	
				31%			28%		41%	
<i>FDI and Pricing are diffusion indexes. At 50, the performance of the category listed met expectatons. A reading above 50 suggests the category outperformed expectatons, while a reading below 50 suggests the category underperformed expectatons.</i>										

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 by the **FCH Sourcing Network** and **Baird** with support from the **National Fastener Distributors Association**. 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. A diffusion index, 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 distributors such as **W.W. Grainger (GWW)** and **MSC Industrial (MSM)**.

Key Points:

FDI results less positive in May. The seasonally-adjusted **May FDI (53.8) decelerated vs. April (55.8)**. Sales trends remained positive, but less so than last month. Exactly 50% of respondents indicated sales were better than seasonal expectations, below 2018 levels (55%) but above weaker YTD results (44%). The pricing index improved on both a m/m and y/y basis, although a majority of respondents still indicated stable pricing levels vs. April. Customer inventory levels continue to be perceived as mostly in line with expectations, while respondents' inventories remain relatively higher.

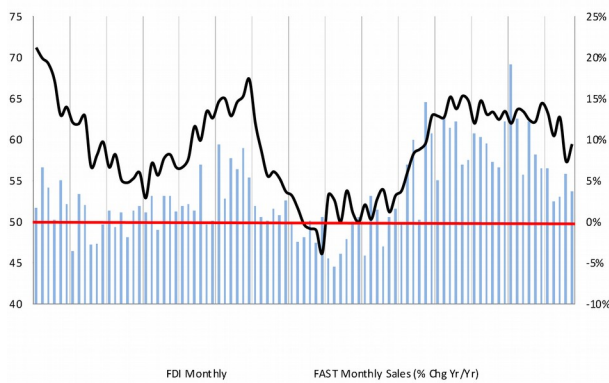
May FLI returns to sub-50 levels. The seasonally-adjusted **FLI contracted m/m (47.7 vs. 52.1)**, returning to sub-50 levels for fourth time in five months this year. Of the FLI's components (employment index, respondent inventories, customer inventories, and six-month outlook), all but the six-month outlook were relatively stable sequentially. The six-month outlook, however, plunged vs. April levels with respondents now seeing contraction on balance in late 2019.

Hiring sentiment mostly unchanged. Hiring sentiment was stable in May as hiring was again in line with to above seasonal expectations for nearly all fastener distributors, consistent with April results. The May US jobs report is scheduled for release Friday, June 7, with economists predicting the overall economy will add 180,000 jobs (vs. 263,000 in April).

Respondent commentary again skews more cautious. There was an uptick in the number of qualitative comments this month, as the tone remains cautious overall. One distributor noted that customers are "ordering for current needs" due to tariff-related fears at present, while another noted "more irregular buying patterns" as compared to the first quarter. Looking forward, one distributor commented they are "hearing about signs of a future downturn" but noted more stable backlog trends, while another predicted slightly slower sales this fall/winter due to an expected "mild recession." As a result, the six-month outlook was less optimistic this month, with just 31% of respondents expecting higher activity levels, 28% expecting similar activity, and 41% expecting lower activity. The percentage of respondents expecting lower activity soared vs. 16% in April, representing the most pessimistic reading since January 2016.

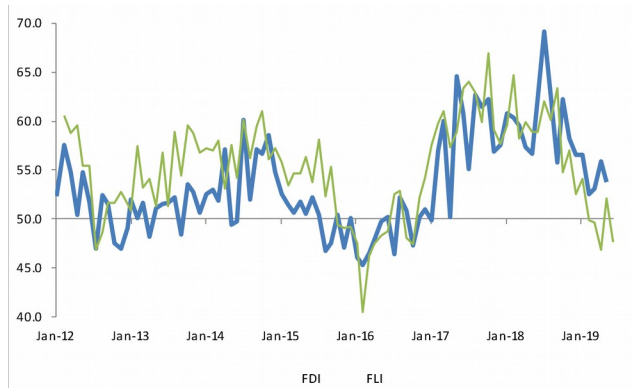
Fastenal reported 9.5% May daily sales growth, slightly below our +9.9% estimate. M/m growth saw benefit from Easter dropping out, while the number of selling days were unchanged both m/m and y/y. Underlying organic growth of +9.9% accelerated ~2% sequentially but still represented the second consecutive month of single-digit organic growth. Fastener growth rebounded somewhat to +8.1% (April +5.1%). Based on FDI data and other research inputs, we continue to expect positive, albeit moderating top-line growth across public industrial distributors in 2019, partially offset by higher pricing.

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.

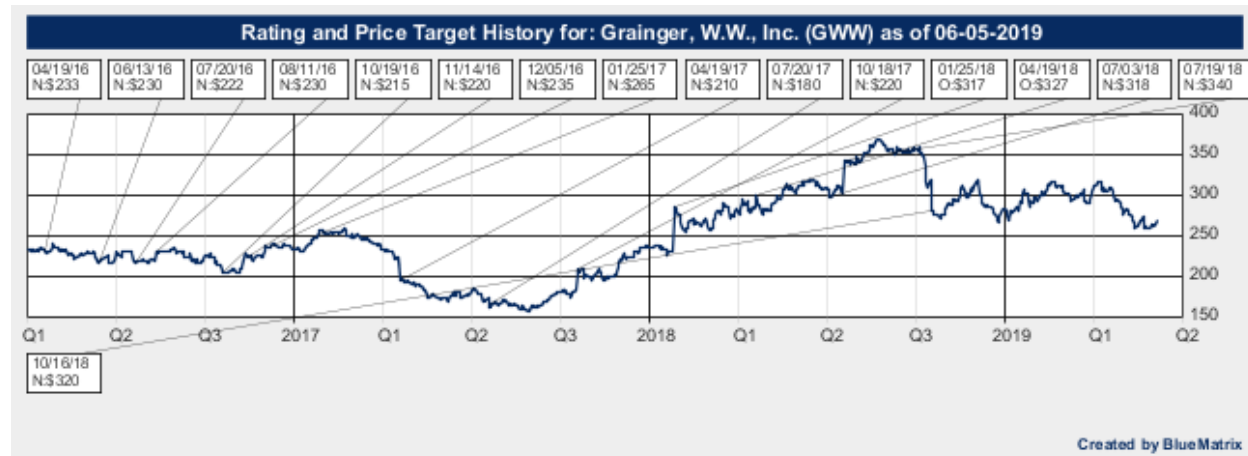
Industrial Distribution: Risks include economic sensitivity, pricing power, online pressure/competitive threats, global sourcing, and exposure to durable goods manufacturing.

Appendix – Important Disclosures and Analyst Certification

Covered Companies Mentioned

All stock prices below are as of 6/6/2019.

Fastenal Company (FAST-\$32.18-Neutral)
 W.W. Grainger Inc. (GWW-\$269.16-Neutral)
 MSC Industrial Direct Co. Inc (MSM-\$72.50-Neutral)
 (See recent research reports for more information)



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