

Fastener Distributor Index – July 2017

Written by R.W. Baird analyst David J. Manthey, CFA 8/5/17



Key Takeaway:

The seasonally-adjusted FDI for July 2017 was 55.1 – decelerating slightly from June’s strong 60.8 reading but remaining well in expansionary territory. Similarly, sales momentum cooled off somewhat from a record reading in June, with a still very strong seasonally-adjusted sales index of 69.8 coming down vs. a record 86.6 last month. Commentary on market conditions was a bit more mixed this month, with some respondents continuing to see growth accelerating, while others noted a slight leveling off of activity. The FDI Forward-Looking Indicator also remains well in expansionary territory, registering a seasonally-adjusted 62.9, but saw a modest deceleration vs. June (64.0).

Key Points:

About the Fastener Distributor Index (FDI). The FDI is a monthly survey of North American fastener distributors, conducted with the **FCH Sourcing Network** and the **National Fastener Distributors Association**. It offers insights into current industry trends/outlooks. As 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 industrial distributors such as **W.W. Grainger (GWW)**, and **MSC Industrial (MSM)**.

July FDI decelerates slightly from June. The seasonally-adjusted July FDI (55.1) ticked down from June’s strong 60.8 reading, mainly driven by a slight moderation in sales momentum relative to a record June. In the July survey, 47% of respondents indicated sales were “better” relative to seasonal expectations, down slightly vs. June (64%). Relative to historical seasonal readings in the month of July, this month’s seasonally-adjusted sales index of 69.8 suggests selling conditions still remain very strong overall. Encouragingly, pricing was higher on a y/y basis for a majority of respondents (53%) – driving the FDI y/y pricing index to the highest level since August 2014. As it relates to customer inventory levels, most respondents believe inventories are relatively in line with expectations (70% of responses), while 30% indicated inventory levels are too low. This compares to June results of 48% and 44%, respectively, as well as 8% who viewed customer inventories as too high in June.

FDI Forwarding-Looking Indicator remains solidly in growth mode. The FDI Forward-Looking Indicator 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. July’s seasonally-adjusted Forward-Looking Indicator ticked down slightly to 62.9 vs. 64.0 in June. The Forward-Looking Indicator averaged 49.7 during 2016, but has averaged 61.0 year-to-date in 2017. Given a solidly expansionary Forward-Looking Indicator and FDI, market conditions appear likely to remain in growth mode in the months ahead.

Manufacturing employment remains stable. Following a notably more bullish turn in hiring sentiment in May, respondents have indicated relatively stable hiring conditions for two straight months. 73% of distributors indicated hiring levels were unchanged relative to seasonal expectations, while 17% saw hiring pick up (vs. 21% in April, 47% in May, and 36% in June). This result in a FDI Employment Index reading of 53.3, down vs. June's strong 68.0 reading but still coming in above the 2016 average (48.9). July's US jobs report, meanwhile, came in solidly above expectations (+209,000 adds vs. +180,000 consensus). Domestic manufacturing employment was up slightly at +16,000 m/m, while average hours per work week for manufacturing employees was flat vs. June (40.9 hours).

July sentiment somewhat mixed. Commentary on current market conditions was more mixed this month vs. recent bullish commentary. Some noted continued strong trends, while others are seeing a possible leveling off of activity levels after several strong months (although nevertheless still solidly higher y/y). As one distributor put it, "The last couple of months things have evened out... not the huge growth of the first several months, but absolutely higher sales than last year." Another respondent characterized July as "slow compared to June," while some attributed a loss of momentum to "more people [taking] time off" in July. Others continue to see consistently strong trends, noting "Sales are picking up and deliveries from some US companies are moving out!" The outlook for the remainder of the year remains largely positive, as 57% of respondents expect higher activity levels over the next six months vs. today, while just 3% expect lower.

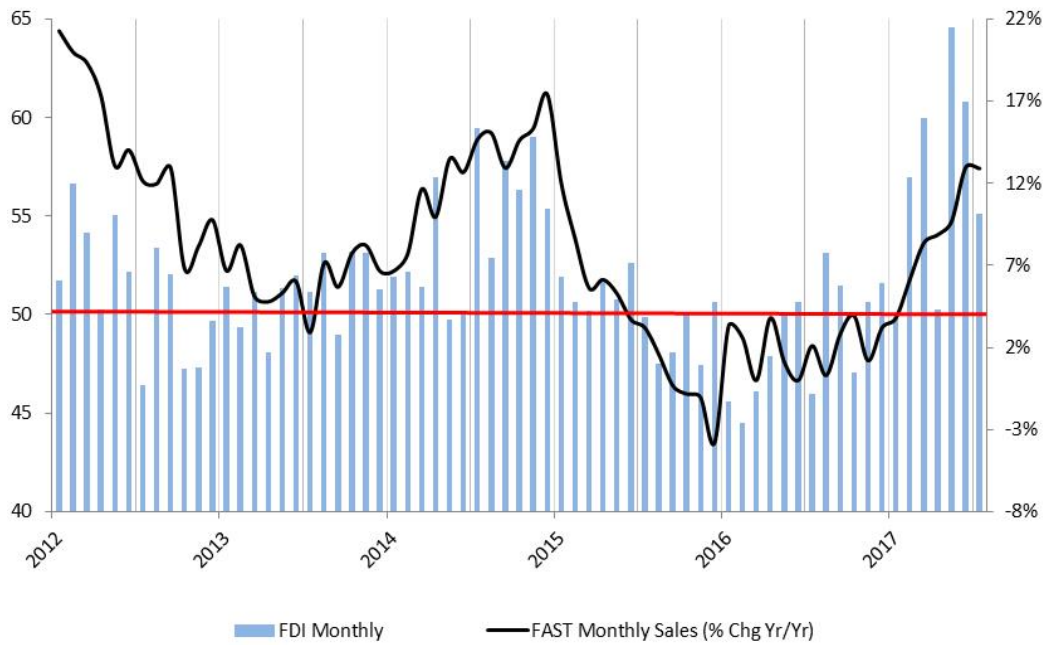
Fastenal reported July daily sales growth of +12.9% y/y, nicely ahead of our +11.5% estimate and reflecting growth in all end markets/product lines. Underlying "core" growth (excluding acquisitions and foreign exchange) was +11.3%, the second consecutive month of double-digit growth. Fasteners saw strong growth at +11.3% y/y, including the recent Mansco acquisition (+7.4% ex-Mansco). Based on FDI data and other research inputs, we continue to expect a substantial uptick in growth among the public industrial distributors this year, with Fastenal daily sales growth expected to average double-digit y/y growth rates for the remainder of 2017.

Fastener Distribution Trends: July 2017

FASTENER DISTRIBUTION AT A GLANCE									
July 2017									
	-----Index Values -----							Directbn	Rate of Change
	Jul	Jun	May	Apr	Mar	Feb	Jan		
PMI (Manufacturing Sector)	56.3	57.8	54.9	54.8	57.2	57.7	56.0	Growing	Slower
FDI (Fastener Sector)	52.9	60.5	66.3	53.7	61.3	55.4	54.5	Growing	Slower
FDI (Seasonally Adjusted)	55.1	60.8	64.6	50.2	60.0	57.0	49.9	Growing	Slower
Sales (SA)	69.8	86.6	79.6	43.8	74.6	62.7	51.6	Growing	Slower
Forward-Looking (SA)	62.9	64.0	63.3	58.9	57.4	61.0	59.8	Growing	Slower
(Other Metrics; NSA)									
Employment	53.3	68.0	73.6	57.4	59.8	62.9	57.6	Growing	Slower
Supplier Deliveries	65.0	64.0	72.2	66.2	61.0	61.4	56.1	Growing	Faster
Respondent Inventories	51.7	52.0	58.3	52.9	61.0	58.6	59.1	Growing	Slower
Customer Inventories	35.0	32.0	36.1	38.2	43.9	40.0	36.4	Declining	Slower
Pricing, month-to-month	65.0	52.0	59.7	60.3	63.4	60.0	62.1	Higher	Faster
Pricing, year-to-year	76.7	66.0	75.0	73.5	72.0	70.0	68.2	Higher	Faster
6-Month Outlook - July			Higher Same		Lower				
			57%		40%		3%		
<i>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.</i>									

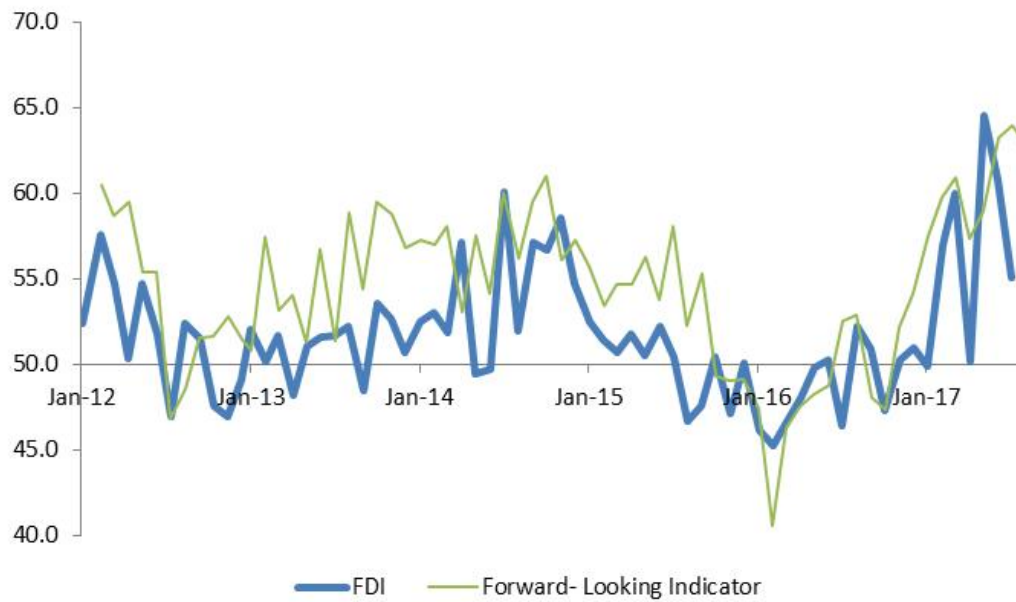
Source: Robert W. Baird & Co., [FCH Sourcing Network](#), Institute for Supply Management

Fastener Distributor Index (FDI); Seasonally Adjusted



Source: Robert W. Baird & Co., FCH Sourcing Network, company reports

FDI vs. Forward-Looking Indicator (Seasonally Adjusted)



Source: Robert W. Baird & Co., FCH Sourcing Network

Appendix – Important Disclosures and Analyst Certification

Covered Companies Mentioned

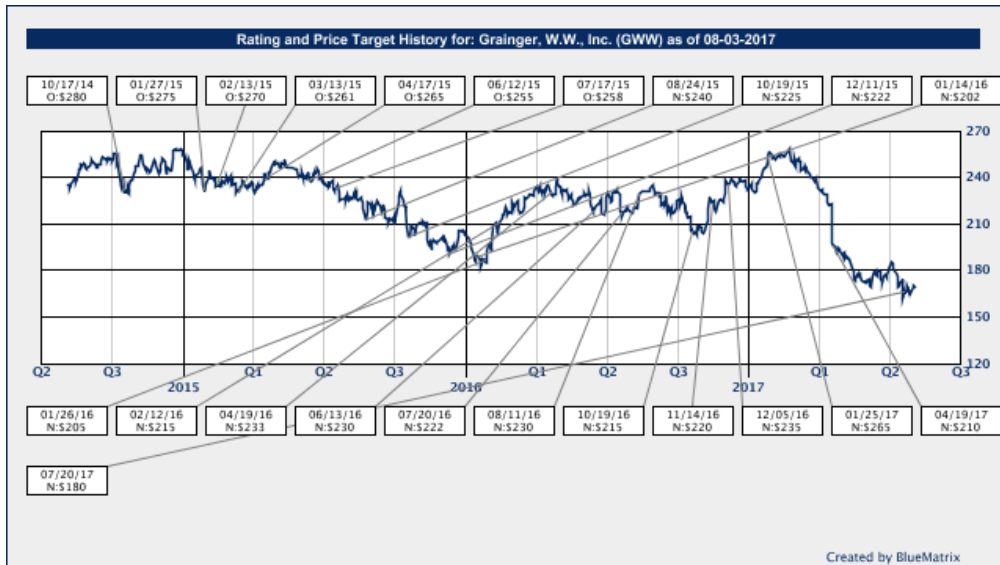
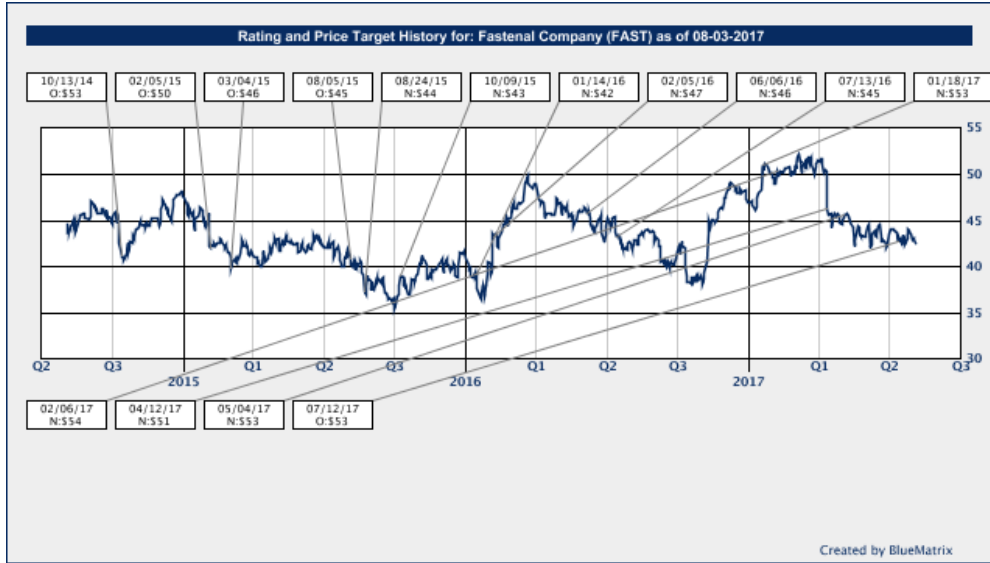
All stock prices below are as of 8/4/2017.

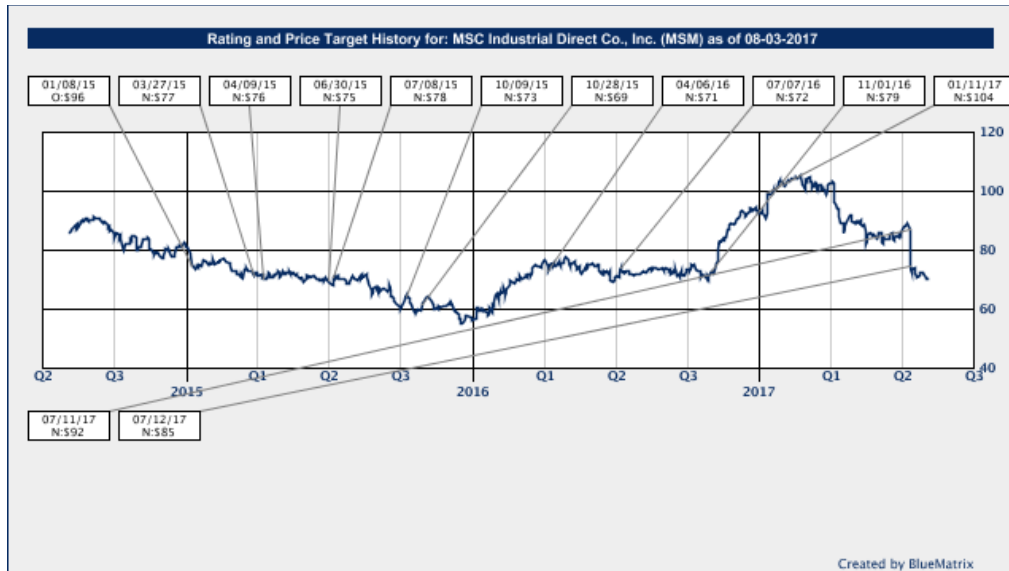
Fastenal Company (FAST- \$43.68)

WW Grainger Inc. (GWW- \$172.07)

MSC Industrial Direct Co. Inc (MSM- \$71.10)

(See recent research reports for more information)





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