

HIGHLIGHTED COVERAGE

Fastenal
FAST - \$45.29 - Hold

W.W. Grainger
GWW - \$229.73 - Hold

MSC Industrial Direct
MSM - \$71.36 - Hold

BB&TCM Fastener Distributor Index (FDI): June Reading Modestly Higher

KEY TAKEAWAY

June's seasonally adjusted FDI reading (50.6) proved modestly higher, as the Index topped 50 for the second time this year (50.1 in May). June results again benefitted from a slight uptick in sales bias among respondents, while employment metrics also showed nascent signs of thawing versus the early year period. While the 50+ reading is encouraging to us, we continue to temper our expectations for more material near-term expansion among fastener distributors. Anecdotes (both public and private) still reflect mixed demand fundamentals and continued top-line headwinds (commodity dislocation, ongoing currency headwinds, mixed industrial production, etc.). We also note the six-month outlook for survey participants remains uncertain, with 52% still expecting unchanged or declining conditions. We will continue watching closely for signs of more tangible strengthening.

KEY POINTS

About the Fastener Distributor Index (FDI). The FDI is a monthly survey of NorAm 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, figures above 50 signal strength, while readings below 50 signal weakness. It should be directly relevant to **Fastenal** and broadly relevant to other distributors (**W.W. Grainger, MSC Industrial**).

June reading modestly encouraging. The seasonally adjusted June FDI (50.6) remained in expansion territory for the second consecutive month, implying nascent stability in the overall environment. Of the items measured (sales, employment, delivery times, inventories, customer inventories), we believe top-line sentiment remains the most compelling indicator in the Index. The seasonally adjusted headline sales reading of 50.8 was the first 50+ reading in 2016. Regarding customer inventories, 14% of participants viewed current levels as "too high". We note that during the headier growth period of 2013-2014, this metric averaged 4%.

Sequential pricing slightly higher. The June sequential point-of-sale pricing index remained in expansion territory (51.7), marking the third month of expansion after topping 50 in April. According to participant commentary last month, higher material costs, to include inflated steel pricing (HRC steel futures +2% in June), could portend continued pricing growth near term (*Bloomberg*). We believe the overall environment for pricing remains notably soft given minimal inflation, although ongoing CPI expansion (+50 bps sequentially in May) remains a modest positive, nonetheless (*Bureau of Labor Statistics*). Last quarter, Fastenal reported fastener price deflation of 1.5%-2%.

Labor sees an unexpected uptick. June employment (58.6) was unexpectedly higher versus May, as 21% of participants noted increased hiring rates sequentially (only 9% higher last month). We believe the early uptick among survey respondents is encouraging given that Fastenal decreased total headcount on an absolute basis by 132 in May. In Q1'16, FAST reiterated its hiring freeze, excluding necessary vending/IT administration adds.

Sentiment still mixed. With the FDI in expansion territory for the second consecutive month, we believe nascent optimism is warranted. As one participant noted, "*Some small positive things (are occurring) in the marketplace...commodity prices moving up very slightly. This is helpful.*" We continue to await more consistent results.

Additional Discussion

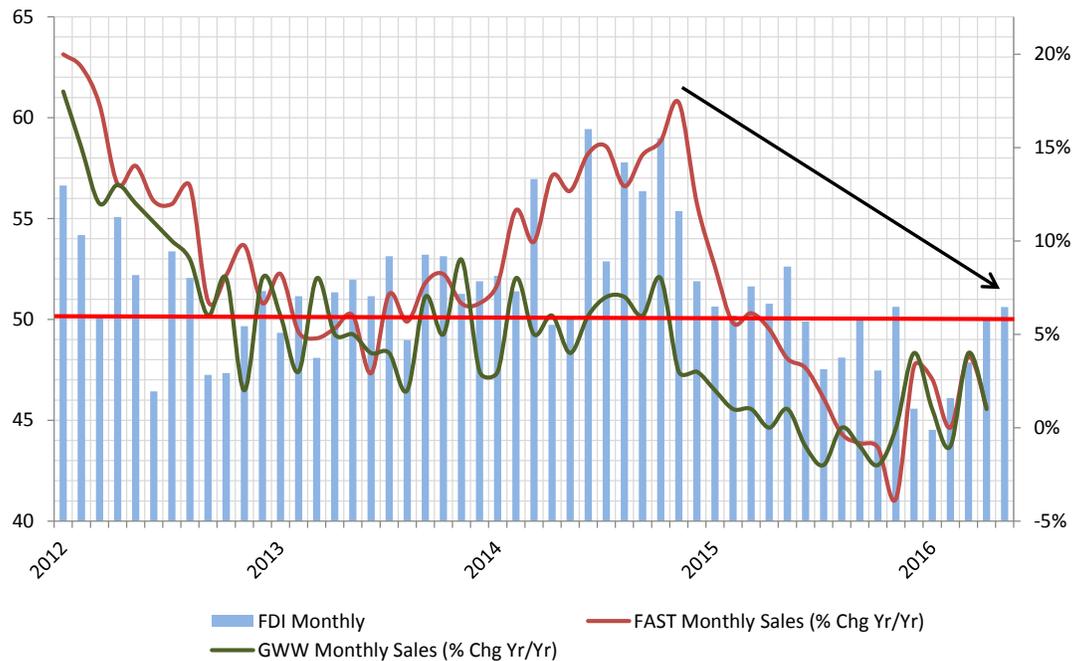
Fastener Distribution Trends; June 2016

FASTENER DISTRIBUTION AT A GLANCE									
June 2016									
	----- Index Values -----						May-->June		
	June	May	Apr.	Mar.	Feb.	Jan.	Change	Direction	
PMI (Manufacturing Sector)	53.2	51.3	50.8	51.8	49.5	48.2	1.9	Growing	
FDI (Fastener Sector)	50.0	51.1	51.3	47.6	44.0	50.4	(1.1)	Declining	
FDI (Seasonally Adjusted)	50.6	50.1	47.9	46.1	44.5	45.6	0.5	Growing	
Sales (SA)	50.8	48.4	38.2	38.6	36.7	36.6	2.5	Growing	
(Other Metrics; NSA)									
Employment	58.6	51.5	51.3	52.4	44.8	46.4	7.1	Growing	
Supplier Deliveries	53.4	54.5	56.6	53.7	51.7	55.4	(1.1)	Slowing	
Respondent Inventories	63.8	68.2	71.1	69.5	69.0	69.6	(4.4)	Too High	
Customer Inventories	43.1	48.5	50.0	41.5	44.8	50.0	(5.4)	Too Low	
Pricing, month-to-month	51.7	51.5	53.9	40.2	43.1	48.2	0.2	Higher	
Pricing, year-to-year	48.3	53.0	47.4	36.6	43.1	41.1	(4.8)	Lower	
<u>Higher</u> <u>Same</u> <u>Lower</u>									
6-Month Outlook - June	48%	24%	28%						

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: BB&TCM, FCH Sourcing Network, Institute for Supply Management

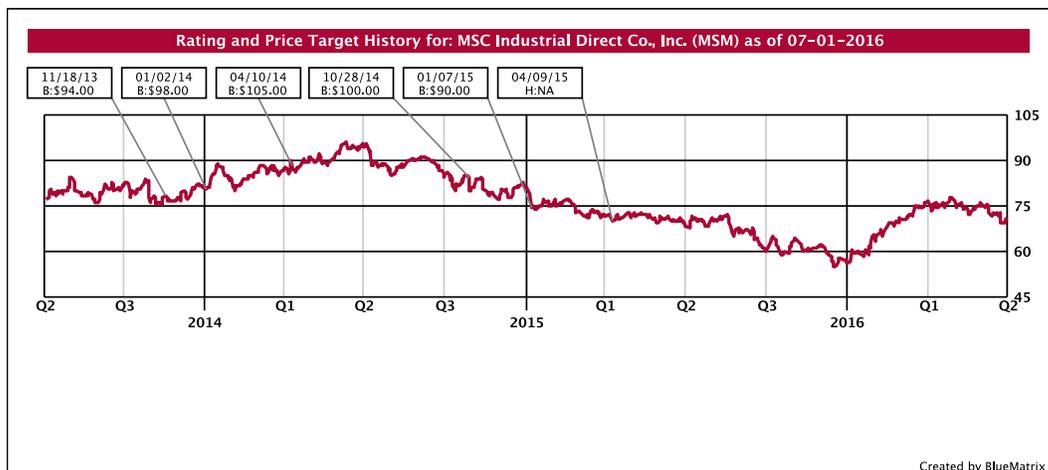
Fastener Distributor Index (FDI); Seasonally Adjusted



Source: BB&TCM, FCH Sourcing Network, company reports

IMPORTANT DISCLOSURES

Price Chart



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All companies under coverage:		All companies under coverage to which it has provided investment banking services in the previous 12 months:	
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Hold (2)	53.01%	Hold (2)	17.84%
Underweight/Sell (3)	3.44%	Underweight/Sell (3)	33.33%
Not Rated (NR)	0.00%	Not Rated (NR)	0.00%

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