

**HIGHLIGHTED COVERAGE****Fastenal**

FAST - \$37.06 - Hold

**W.W. Grainger**

GWW - \$223.73 - Hold

**MSC Industrial Direct**

MSM - \$63.46 - Hold

**BB&TCM Fastener Distribution Index (FDI)- Reflects Sluggish September Sales****KEY TAKEAWAY**

The FDI is a monthly survey of NorAm fastener distributors that aims to provide insight into current trends/outlooks. As a diffusion index, readings above 50 signal strength and below 50 signal weakness. For the third consecutive month, the seasonally adjusted September FDI fell below 50 (47.5), which we believe is consistent with the tough current environment for many distributors. Added contraction was driven by the lowest seasonally adjusted sales figure (32.4) yet recorded for the FDI. In addition, employment fell into contraction for the first time since April 2013. Sequential uptick in the aggregate index resulted from a normalization of customer inventories, which remained in negative territory (43.6). Pricing and supplier deliveries were largely unchanged, and the long-term outlook for industry sentiment ticked modestly lower. Overall, we believe that fastener distributors continue to face material demand pressure from lower commodity prices, forex, and weaker industrial production. We maintain our cautious outlook on the industry, but will continue to watch for signs of more material long-term improvement.

**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**).

**September sales sentiment plunges.** For September, the FDI fell below 50 (47.5) for the third consecutive month. Of the items measured (sales, employment, delivery times, inventories, customer inventories), we believe weaker top-line sentiment remains the most directionally accurate indicator in the Index. 85% of total respondents reported sequentially flat or lower sales for September. In our view, the results are consistent with sluggish recent growth from Fastenal (+1.6% yr/yr in August versus a five year average of +13.2%), Grainger (-2% in August versus FY'15 guide of 0%-2%), and MSC (company estimated +2.2% in June versus +7.6% last year).

**Employment also contracts.** Of additional note, the September employment index (48.7) showed a contraction in overall headcount for select distribution respondents for the first time in 30 months. We believe these results are consistent with recent contraction from Fastenal, which reduced total headcount on an absolute basis in August for the first time in seven months. Additionally, Fastenal continues to consolidate select branch locations (-3% yr/yr), which we believe reflects the tepid overall demand environment.

**Pricing largely stagnant.** Point-of-sale pricing for September was unchanged versus August for 74% of survey participants. We believe the overall environment for price increases remains notably soft given material demand pressure (declining commodity prices, forex, weaker industrial production) and minimal inflation. Additionally, we view the survey results as largely consistent with recent price adjustments from Grainger (-1% in Q2'15).

**What does this mean for public distributors?** In our view, the data reflects overall weakness within the domestic economy, and 2015 has proven difficult thus far for many industrial distributors. We believe lower energy spending is at the root of weaker sales, with currency woes further compounding the slowdown. Recent conversations with private industry contacts suggest continued pressure on manufacturing demand for the latter portion of FY'15 (69% of FDI respondents expect flat-to-weaker conditions six months from now). We will continue to watch for signs of more material long-term improvement. For now, however, we expect announced earnings for Fastenal (10/13) and Grainger (10/16) to reflect ongoing weakness in the overall industrial environment.

**Additional Discussion**

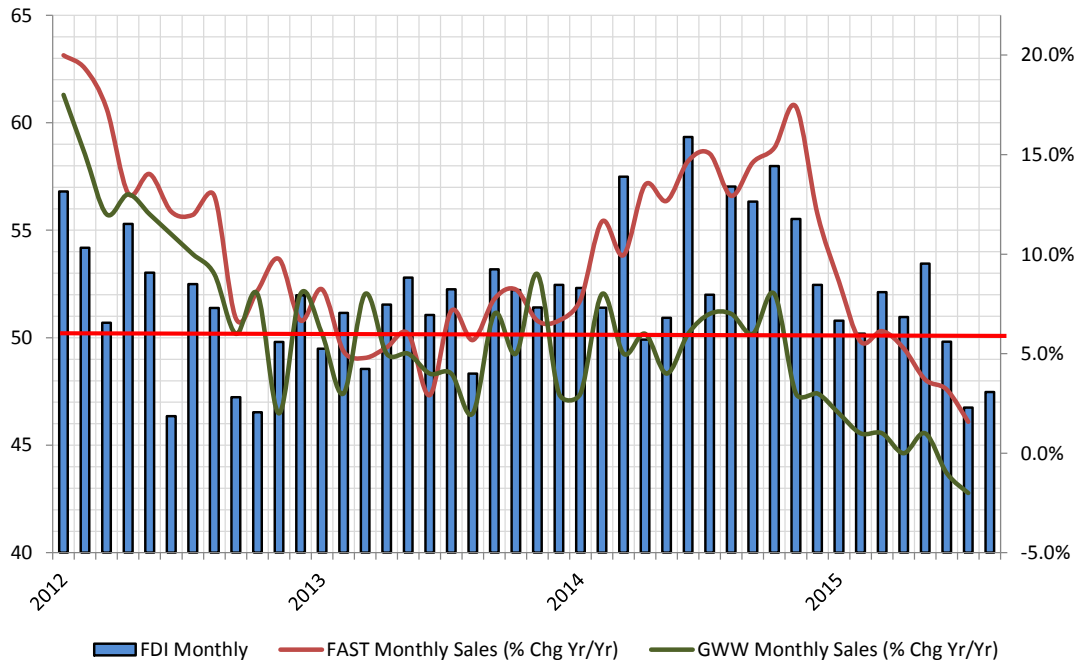
**Fastener Distribution Trends; September 2015**

FASTENER DISTRIBUTION AT A GLANCE									
September 2015									
	----- Index Values -----						Aug.-->Sep.		
	Sep.	Aug.	Jul.	Jun.	May	Apr.	Change	Direction	
PMI (Manufacturing Sector)	50.2	51.1	52.7	53.5	52.8	51.5	(0.9)	Growing	
FDI (Fastener Sector)	44.6	45.5	48.4	52.0	51.9	55.4	(0.9)	Declining	
<b>FDI (Seasonally Adjusted)</b>	<b>47.5</b>	<b>46.7</b>	<b>49.8</b>	<b>53.4</b>	<b>51.0</b>	<b>52.1</b>	<b>0.7</b>	<b>Declining</b>	
Sales (SA)	32.4	45.3	35.4	68.7	53.3	58.3	(12.9)	Declining	
<b>(Other Metrics; NSA)</b>									
Employment	48.7	52.3	52.1	60.5	53.7	54.8	(3.6)	Declining	
Supplier Deliveries	56.4	56.8	58.3	57.9	66.7	57.1	(0.4)	Slowing	
Respondent Inventories	67.9	70.5	64.6	55.3	57.4	50.0	(2.5)	Too High	
Customer Inventories	43.6	29.5	50.0	34.2	33.3	40.5	14.0	Too Low	
Pricing, month-to-month	44.9	45.5	45.8	55.3	50.0	54.8	(0.6)	Lower	
Pricing, year-to-year	51.3	54.5	58.3	71.1	68.5	83.3	(3.3)	Higher	
<u>Higher</u> <u>Same</u> <u>Lower</u>									
6-Month Outlook - Sept.	31%	38%	31%						

*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

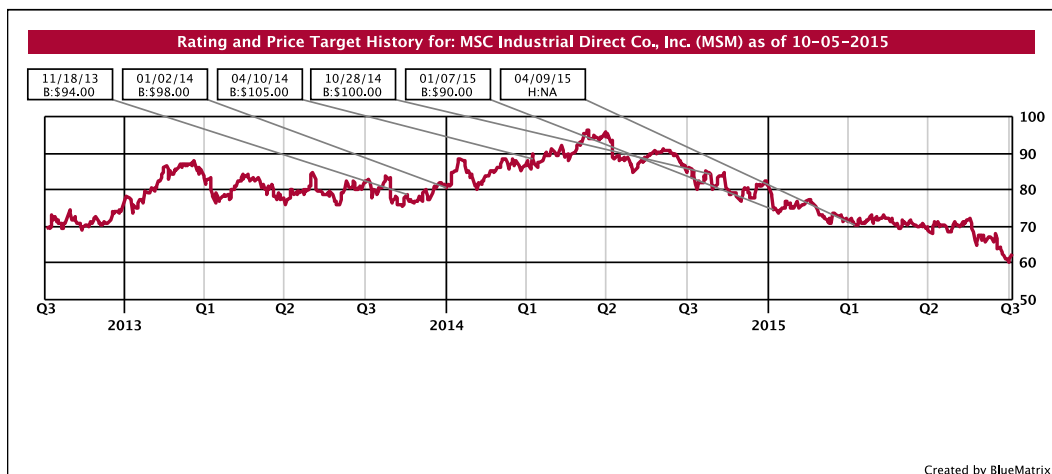
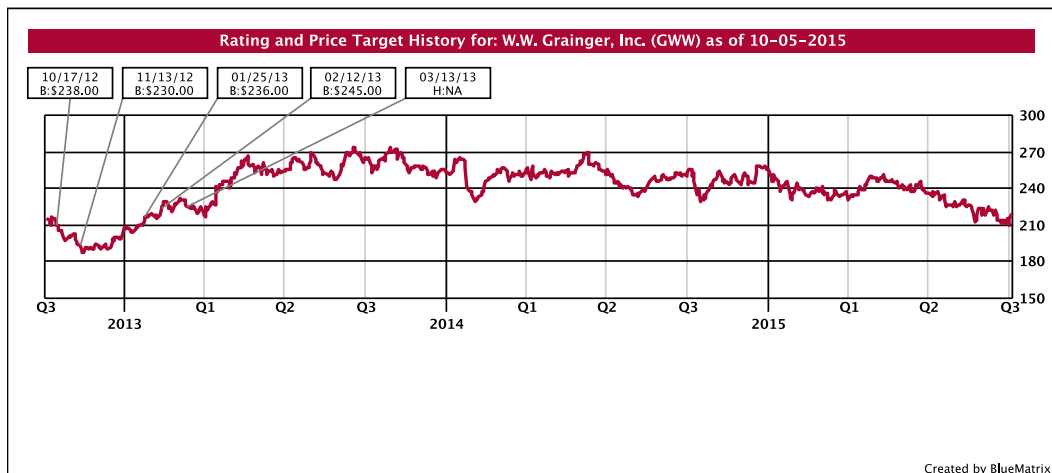
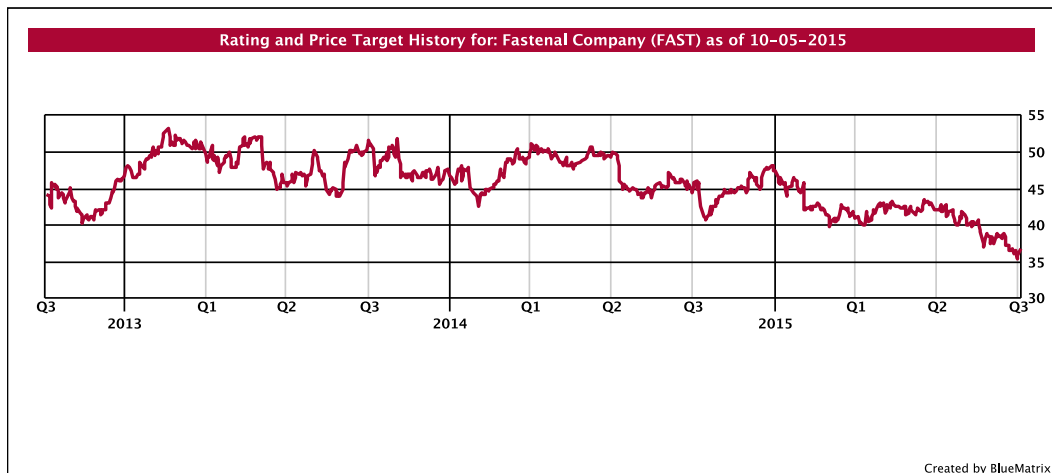
**Fastener Distributor Index (FDI); Seasonally Adjusted**



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

## IMPORTANT DISCLOSURES

### Price Chart



#### BB&T Capital Markets rating distribution by percentage (as of October 7, 2015):

All companies under coverage:

Buy (1)	44.59%
Hold (2)	55.08%
Underweight/Sell (3)	0.33%
Not Rated (NR)	0.00%

All companies under coverage to which it has provided investment banking services in the previous 12 months:

Buy (1)	26.47%
Hold (2)	19.05%
Underweight/Sell (3)	0.00%
Not Rated (NR)	0.00%

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The definition of each rating is as follows:

Buy (1): estimated total return potential greater than or equal to 10%, Hold (2): estimated total return potential greater than or equal to 0% and less than 10%, Underweight (3): estimated total return potential less than 0%

**B:** Buy **H:** Hold **UW:** Underweight **NR:** Not Rated **NA:** Not Applicable **NM:** Not Meaningful **SP:** Suspended

Stocks rated Buy (1) are required to have a published 12-month price target, while it is not required on stocks rated Hold (2) and Underweight (3).

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