

HIGHLIGHTED COVERAGE

Fastenal
FAST - \$47.37 - HoldW.W. Grainger
GWW - \$231.26 - HoldMSC Industrial Direct
MSM - \$75.45 - Hold**BB&TCM Fastener Distributor Index (FDI): Improving Sales Bias Encouraging****KEY TAKEAWAY**

For March, the seasonally adjusted FDI (46.1) remained in contraction territory, yet responses on the aggregate ticked slightly higher versus the prior month (44.5). While we believe the environment for both distributors and manufacturers remains largely strained, 59% of March respondents noted similar or better sequential sales growth, up from 41% in February. Hiring sentiment was also modestly improved, while responses involving pricing, deliveries, and inventory were again cautious. Despite the headline contraction, we are encouraged by the early improvement in sales bias among our survey participants. We also note that select ancillary macro indicators (IP/PMI) have shown renewed life in recent readings, perhaps suggesting stronger conditions in the months ahead. We will continue to watch closely for added 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**).

Was February the FDI trough? Sales uptick modestly encouraging. The March FDI (46.1) implies continued contraction in overall growth conditions, although declines stabilized versus February (44.5). Of the items measured (sales, employment, delivery times, inventories, customer inventories), we believe top-line sentiment remains the most compelling indicator in the Index. To the positive, 59% of March respondents noted similar or better sequential sales growth, up from 41% in February. The employment component of the FDI (52.4) also ticked higher in March, as 90% of participants noted unchanged or improving hiring conditions versus the preceding month. Regarding customer inventories, 20% of participants viewed current levels as "too high." We note that during the headier growth period of 2013-2014, this metric averaged 4%.

Pricing still unchanged. Point-of-sale pricing for March was unchanged versus December for 71% of survey participants (24% lower). 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 results as largely consistent with recent yr/yr price adjustments from Grainger (-2% in February) and Fastenal (-2% on fasteners last quarter). MSC has proven to be an outlier here, with modest price realization partially attributed to nascent traction on supplier discounts and renewed freight initiatives. MSC reports Q2'16 results on 4/6.

Select macro indicators picking up steam. We continue to see early divergence between the FDI and select macro readings, to include IP and ISM/PMI. We believe a stronger March PMI (51.8, the first 50+ reading since last August) could bode well for better results from our private fastener distributors in the coming months (*Institute for Supply Management*). Among the major publicly-traded distributors, early year sales growth from Grainger and Fastenal has also been modestly encouraging, in our view, and yr/yr comps become increasingly favorable later in FY'16.

Overall: Survey still suggests caution. Anecdotal survey commentary points to choppy near-term demand for many fastener-centric distributors in H1'16, with the potential for more substantive growth in H2'16. As one participant noted, "*The marketplace is still very volatile and unpredictable...just no true pattern to predictability.*" Lower energy spending is at the root of weaker sales for many providers, in our view, with currency woes further compounding the slowdown. Despite the noted concern, we view the early sales uptick (along with the stronger ancillary macro readings) as a potential catalyst for better conditions ahead.

Additional Discussion

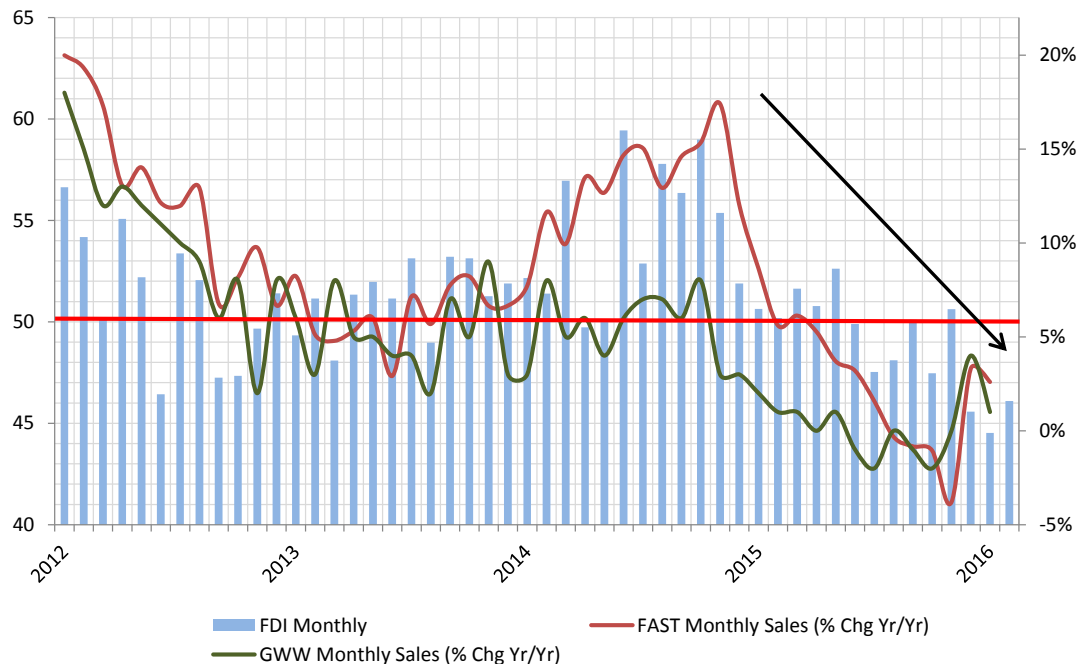
Fastener Distribution Trends; March 2016

FASTENER DISTRIBUTION AT A GLANCE								
March 2016								
	----- Index Values -----						Feb.-->Mar.	
	Mar.	Feb.	Jan.	Dec.	Nov.	Oct.	Change	Direction
PMI (Manufacturing Sector)	51.8	49.5	48.2	48.0	48.4	49.4	2.3	Growing
FDI (Fastener Sector)	47.6	44.0	50.4	49.4	46.2	49.6	3.6	Declining
FDI (Seasonally Adjusted)	46.1	44.5	45.6	50.6	47.5	50.1	1.6	Declining
Sales (SA)	38.6	36.7	36.6	50.4	37.0	48.3	1.9	Declining
(Other Metrics; NSA)								
Employment	52.4	44.8	46.4	48.8	50.0	53.1	7.6	Growing
Supplier Deliveries	53.7	51.7	55.4	55.0	59.1	51.6	1.9	Slowing
Respondent Inventories	69.5	69.0	69.6	68.8	68.2	65.6	0.5	Too High
Customer Inventories	41.5	44.8	50.0	50.0	45.5	42.2	(3.4)	Too Low
Pricing, month-to-month	40.2	43.1	48.2	45.0	42.4	43.8	(2.9)	Lower
Pricing, year-to-year	36.6	43.1	41.1	50.0	48.5	53.1	(6.5)	Lower
<u>Higher</u> <u>Same</u> <u>Lower</u>								
6-Month Outlook - Mar.	37%	32%	32%					

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

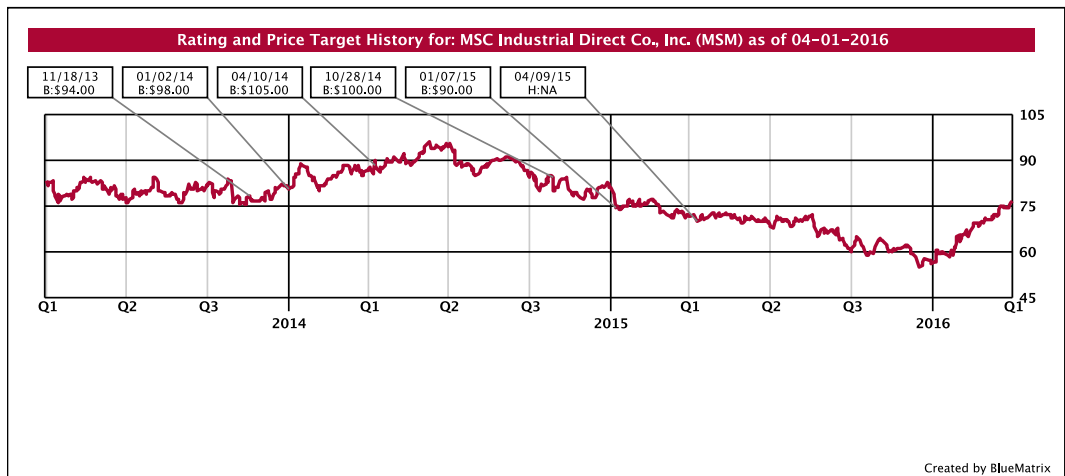
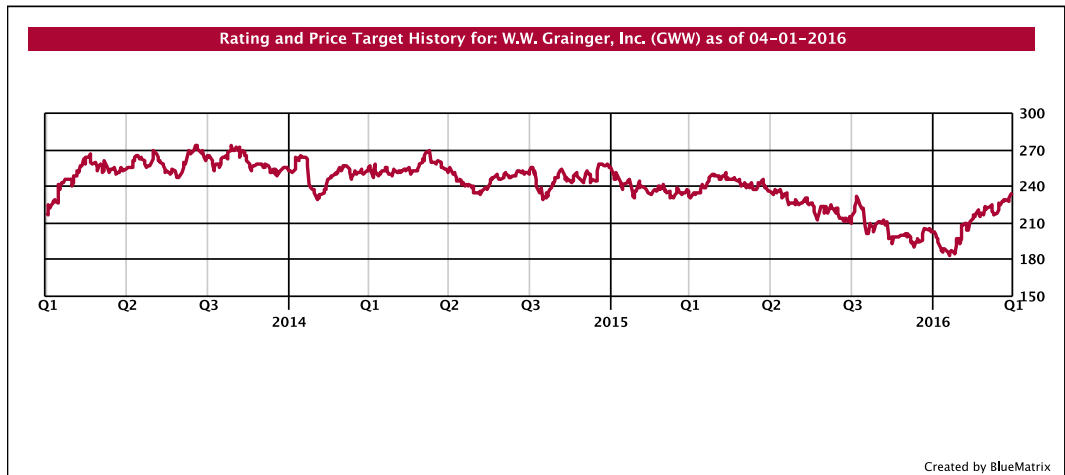
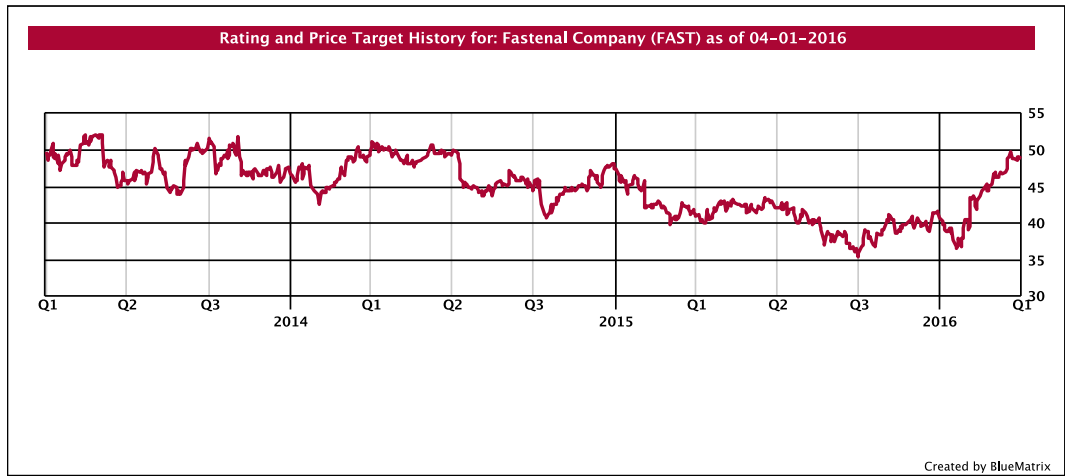
Fastener Distributor Index (FDI); Seasonally Adjusted



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:	
Buy (1)	43.02%	Buy (1)	29.05%
Hold (2)	53.49%	Hold (2)	16.85%
Underweight/Sell (3)	3.49%	Underweight/Sell (3)	33.33%
Not Rated (NR)	0.00%	Not Rated (NR)	0.00%

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