

## COMPANIES MENTIONED

## Fastenal

FAST - \$48.04 - Hold

## W.W. Grainger

GWW - \$208.42 - Buy

## MSC Industrial Direct

MSM - \$78.29 - Hold

**BB&TCM's Fastener Distributor Index (FDI) - Bidding Time Until Q1'13  
In December****KEY TAKEAWAY**

The investment narrative has been a difficult Q4'12 due to destocking and plant shutdowns with the potential for a better start to 2013 as these issues faded. The FDI seemed to bear this out in November, and results were eerily similar in December. The FDI was in marginal contraction territory again, with the current sales component being in awful shape. But the outlook statement was increasingly positive again, and respondents are looking for growth in 2013. Overall, the FDI seems to fully support the narrative. Q1'13 will be a key set of readings.

**KEY POINTS**

**About the Fastener Distributor Index (FDI).** The FDI is a monthly survey of NorAm fastener distributors, conducted with the **FCH Sourcing Network**, which offers insights into current trends/outlooks. As a diffusion index, figures above 50 signal strength and below 50 signal weakness. It should be directly relevant to Fastenal and broadly relevant to other distributors (W.W. Grainger, MSC Industrial).

**December (48.4, vs. 46.1 in Nov.) replicates November's results.** Results were eerily similar month-to-month in terms of total number *and* composition. Sales were poor (32.8) but not materially worse than November (34.4) while the three other elements (Employment, Supplier Deliveries, Customer Inventories) were a bit stronger. Poor sales are never welcome, but nor is it all that big a surprise: we have highlighted worries over destocking and plant shutdowns afflicting Q4'12, and this would simply seem to be confirmation of that. *December, like November, was not particularly good, but that was not particularly surprising to us either.*

**Also like November, the December outlook is increasingly positive.** Again, a poor current environment did not dampen enthusiasm for H1'13. More respondents in December are expecting activity to be higher in six months (55%, vs. 47% in Nov.) than lower (23%, vs. 25% in Nov.). This is the first time more than half of respondents had a favorable view of the future since April. *This continues to fit the narrative of an economy in a lull before firming up a bit in 2013.*

**Pricing: none, but it didn't go negative.** In November we believed pricing was "flattish". We believe the same result was evident in December, but there was some marginal improvement in all the pricing indices. *Expectations for pricing are rightly low, in our view. The drama involved whether recent moderation would spill into negative territory. We would take it as a positive that it did not in December.*

**Supplemental query: expected growth in 2013?** We simply asked respondents what level of sales growth they expected in 2013, and what portion of that was expected to be price. The weighted average results: sales +4% and pricing +1%.

**What does this mean for the "Big 3" distributors?** No change from November: December builds on already tough Q4'12 results. This may be mitigated at Grainger by its clean-up/recovery after Hurricane Sandy and MRO orientation. But for purer production names, Fastenal and MSC Industrial, it reinforces the risk of a poor Q4'12. Again, this has been widely expected and the outlook statement suggests to us the problem lies not with baseline demand but with transitory issues that should fade as we enter 2013. Time will tell.

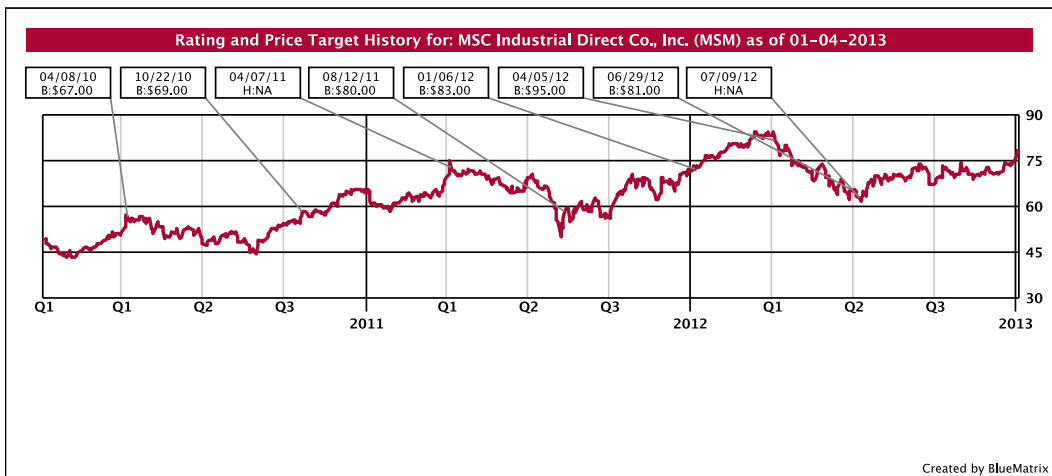
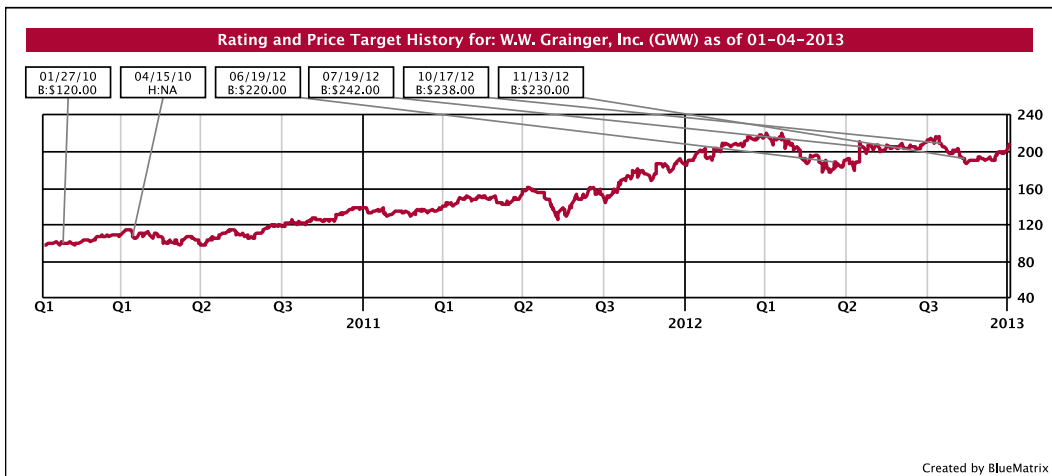
| FASTENER DISTRIBUTION AT A GLANCE  |                 |                 |                 |                  |                   |                 |                       |           |
|------------------------------------|-----------------|-----------------|-----------------|------------------|-------------------|-----------------|-----------------------|-----------|
| December 2012                      |                 |                 |                 |                  |                   |                 |                       |           |
|                                    | Index -<br>Dec. | Index -<br>Nov. | Index -<br>Oct. | Index -<br>Sept. | Index -<br>August | Index -<br>July | Nov.-->Dec.<br>Change | Direction |
| <b>PMI (Overall mfring sector)</b> | 50.7            | 49.5            | 51.7            | 51.5             | 49.6              | 49.8            | 1.2                   | Growing   |
| <b>FDI (Fastener distribution)</b> | 48.4            | 46.1            | 46.8            | 48.2             | 51.0              | 45.1            | 2.3                   | Declining |
| Sales                              | 32.8            | 34.4            | 48.6            | 45.7             | 51.4              | 38.2            | (1.6)                 | Declining |
| Employment                         | 53.1            | 50.0            | 51.4            | 51.4             | 54.2              | 50.0            | 3.1                   | Growing   |
| Supplier Deliveries                | 60.9            | 56.3            | 48.6            | 50.0             | 52.8              | 51.3            | 4.7                   | Slowing   |
| Respondent Inventories             | 64.1            | 59.4            | 62.9            | 62.9             | 62.5              | 57.9            | 4.7                   | Too High  |
| Customer Inventories               | 46.9            | 43.8            | 38.6            | 45.7             | 45.8              | 40.8            | 3.1                   | Too Low   |
| Pricing, month-to-month            | 51.6            | 48.4            | 50.0            | 47.1             | 52.8              | 55.3            | 3.1                   | Higher    |
| Pricing, year-to-year              | 57.8            | 53.1            | 58.6            | 55.7             | 66.7              | 61.8            | 4.7                   | Higher    |
|                                    | <u>Higher</u>   | <u>Same</u>     | <u>Lower</u>    |                  |                   |                 |                       |           |
| 6-Month Outlook - Dec.             | 55%             | 23%             | 23%             |                  |                   |                 |                       |           |

*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.*

Sources: BB&T Capital Markets, FCH Sourcing Network, Institute for Supply Management

**IMPORTANT DISCLOSURES**

**Price Chart**



**BB&T Capital Markets rating distribution by percentage (as of January 7, 2013):**

|                               |        |  |        |
|-------------------------------|--------|--|--------|
| All companies under coverage: |        | All companies under coverage to which it has provided investment banking services in the previous 12 months: |        |
| Buy (1)                       | 46.50% | Buy (1)  | 15.69% |
| Hold (2)                      | 52.28% | Hold (2)   | 5.23%  |
| Underweight/Sell (3)          | 1.22%  | Underweight/Sell (3)   | 0.00%  |
| Not Rated (NR)                | 0.00%  | Not Rated (NR)   | 0.00%  |

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The definition of each rating is as follows:

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