

COMPANIES MENTIONED

Fastenal
FAST - \$43.80 - Hold**W.W. Grainger**
GWW - \$201.06 - Buy**MSC Industrial Direct**
MSM - \$71.88 - Hold**BB&TCM's Fastener Distributor Index (FDI) - October Better Than the Headline****KEY TAKEAWAY**

BB&TCM's Fastener Distribution Index (FDI) fell to 46.8 in October, below September's 48.2. Yet, the details are not as bad as the headline number. The Sales piece improved on September and a big drag was Customer Inventories which is not good (suggests inventory culling in October) but could set the table for future restocking, in our view. Thus, we continue to see results signaling stabilization of demand. Not a great headline, and no one should mistake October's FDI as robust. But it does not seem to be signaling sustained erosion either.

KEY POINTS

About the Fastener Distributor Index (FDI). The FDI is a monthly survey of NorAm fastener distributors, conducted in partnership with the FCH Sourcing Network, which aims to provide insights into current trends/outlooks. As a diffusion index, readings 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).

October's headline not great (46.8, vs. 48.2 in September), but details are better. As in September, technically fastener distributors saw conditions worsen in October. But as in September, we think the details offer a better picture than the headline. For instance, while the overall index worsened, the Sales component (48.6, vs. 45.7 in September) improved, posting its second highest reading of the last five months. Also, a big drag was Customer Inventories (38.6, vs. 45.7 in September). This is not good, of course, but to the extent customers are culling inventories it sets the table for purchasing to improve once that process is complete, so seems a bit short term, in our view. *The figure suggests some short-term pressure continues owing to inventory destocking, but offers no hint that baseline demand worsened any in October. We would still argue the space is in a sluggish equilibrium.*

The 6-month outlook: an increasing absence of pessimism. In October, 34% of respondents anticipated activity to be higher in six months; this is essentially not changed from September (31%). Where there was a change was that respondents fled from the camp expecting lower results (14%, vs. 26% in September) to the "same" camp (51%, vs. 43% in September). *Another signal of stabilization.*

Pricing: no change. In October, the sequential index was 50, suggesting no change. In the last three months it has averaged 50.0, signaling the same. Annual pricing is still higher, but at a narrowing rate that the survey suggests is in the 0.5%-1.5% range. *On the whole, there appears to be little impetus for fresh pricing in fasteners.*

The supplemental question: what about discounting? We believe this survey has made clear that pricing in the fastener industry is stable. But pricing is just one part of the equation. What about discounting? Well, it would appear to be similarly balanced. Asked about it, most respondents (48.6%) said it was no better/worse than normal while the balance was split exactly equally (25.7% on both sides) between getting worse and getting better. *Taken as a whole, price competition does not seem to be worsening in the fastener space at this stage.*

What does this mean for the "Big 3" distributors? The result suggests October results for Fastenal, Grainger, and MSC Industrial are trending slightly below seasonal norms, not because the macro environment "feels" worse but because of inventory culling. Still, that process may be followed with longer plant shutdowns in December which together might generate a softer looking Q4'12.

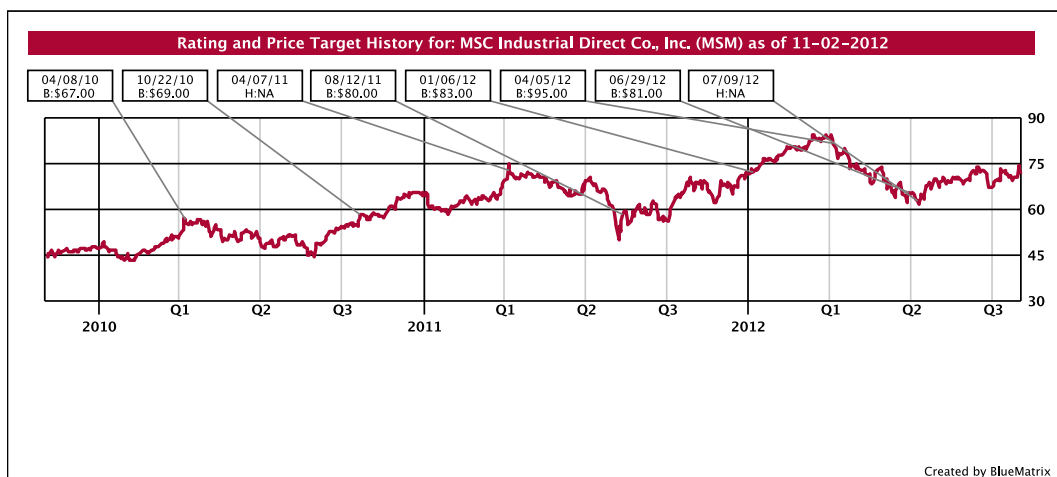
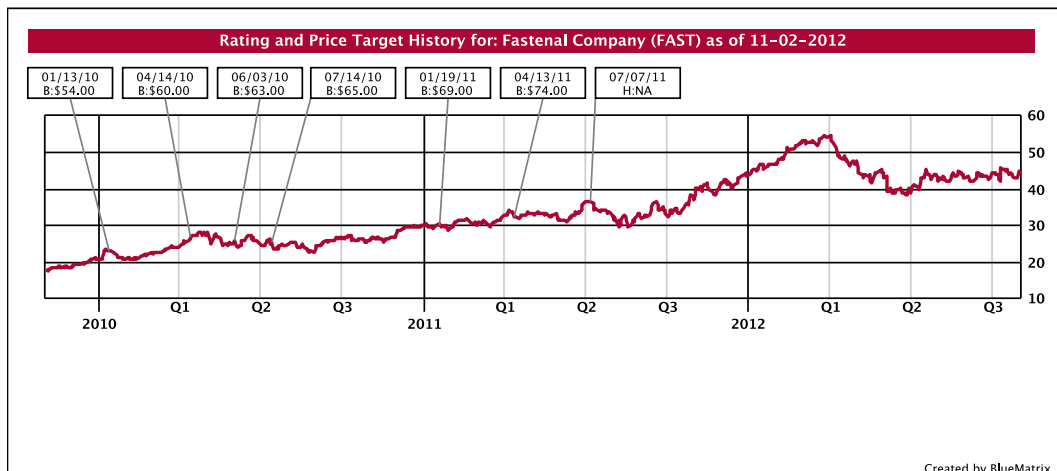
FASTENER DISTRIBUTION AT A GLANCE												
October 2012												
	Index - Oct.	Index - Sept.	Index - August	Index - July	Index - June	Index - May	Index - Apr.	Index - Mar.	Index - Feb.	Index - Jan.	Sep. --> Oct. Change	Direction
PMI (Overall mfring sector)	51.7	51.5	49.6	49.8	49.7	53.5	54.8	53.4	52.4	54.1	0.2	Growing
FDI (Fastener distribution)	46.8	48.2	51.0	45.1	51.6	56.3	53.8	55.9	55.9	57.3	(1.4)	Declining
Sales	48.6	45.7	51.4	38.2	42.2	58.8	55.1	69.4	64.5	79.1	2.9	Declining
Employment	51.4	51.4	54.2	50.0	54.7	58.8	59.0	63.9	59.2	58.1	0.0	Growing
Supplier Deliveries	48.6	50.0	52.8	51.3	60.9	61.3	59.0	48.6	52.6	52.3	(1.4)	Speeding Up
Respondent Inventories	62.9	62.9	62.5	57.9	60.9	55.0	62.8	59.7	53.9	58.1	0.0	Too High
Customer Inventories	38.6	45.7	45.8	40.8	48.4	46.3	42.3	41.7	47.4	39.5	(7.1)	Too Low
Pricing, month-to-month	50.0	47.1	52.8	55.3	57.8	51.3	55.1	61.1	57.9	50.0	2.9	Lower
Pricing, year-to-year	58.6	55.7	66.7	61.8	56.3	65.0	70.5	70.8	71.1	65.1	2.9	Higher
	<u>Higher</u>	<u>Same</u>	<u>Lower</u>									
6-Month Outlook - Oct.	34%	51%	14%									

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&T Capital Markets' estimates, FCH Sourcing Network, Institute for Supply Management

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Price Chart



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Not Rated (NR)	0.00%	Not Rated (NR)	0.00%

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NR: Not Rated **NA:** Not Applicable **NM:** Not Meaningful **SP:** Suspended

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COMMERCIAL AND INDUSTRIAL

Building Materials

John F. Kasprzak Jr. (804) 782-8715
 Paul Betz, CFA (804) 782-8746
 Teresa T. Nguyen, CFA (804) 782-8745

Commercial Durables

Matthew S. McCall, CFA (804) 780-3582
 Vineet Khanna (804) 482-7111

Industrial Equipment - Distribution & Components

Holden Lewis (703) 471-3894
 John C. Cooper (804) 787-8293

Industrial Equipment - Flow Control

Kevin R. Maczka, CFA (804) 782-8811
 Nicholas V. Prendergast (804) 782-2006

Industrial Equipment - Machinery

C. Schon Williams (804) 782-8769
 Aaron M. Reeves (804) 780-3237

Specialty Construction/Environmental Services

Adam R. Thalhimier, CFA (804) 344-8377
 Charles E. Redding (804) 782-8853

CONSUMER

Agribusiness/Consumer Foods

Heather L. Jones (804) 780-3280
 Brett M. Hundley, CFA (804) 782-8753
 Harsh Nahata (804) 482-5775

Apparel, Footwear, & Specialty Retail

Scott D. Krasik, CFA (212) 822-8138
 Kelly L. Halsor, CFA (212) 822-8132

Automotive Aftermarket

Bret D. Jordan, CFA (617) 316-1345
 David L. Kelley (617) 316-1344

Food & Drug Merchandising

Andrew P. Wolf, CFA (804) 787-8224
 Ashby W. Price (804) 782-8711

Specialty Hardlines Retailers

Anthony C. Chukumba (212) 822-8143
 Eric Cohen (212) 822-8140

ENERGY

Coal

Mark A. Levin (804) 782-8856
 Nathan P. Martin (804) 782-8799
 Garrett S. Nelson (804) 787-8259

Diversified Mining

Garrett S. Nelson (804) 787-8259
 Nathan P. Martin (804) 782-8799

Energy Infrastructure

Robert F. Norfleet III (804) 787-8231
 John Ellison (804) 782-8732

FINANCIAL SERVICES

Banks/Thriffs

Cary A. Morris (804) 782-8831
 Blair C. Brantley, CFA (804) 727-2604

Specialty Finance

Vernon C. Plack, CFA (804) 780-3257
 Peter W. Council, CFA (804) 782-8850

TECHNOLOGY

Aerospace

F. Carter Leake (804) 482-7167
 John C. McLeod (804) 225-5899

Commercial IT Services/Government Services

George A. Price Jr. (703) 471-3892
 Jethro R. Solomon (703) 471-3893

Defense

Jeremy W. Devaney (703) 471-3891

TRANSPORTATION SERVICES

Airfreight & Logistics/Maritime

Kevin W. Sterling, CFA (804) 782-8804
 William W. Horner (804) 787-1143
 Chip Rowe (804) 782-8787

Railroads

Mark A. Levin (804) 782-8856
 Nathan P. Martin (804) 782-8799
 Garrett S. Nelson (804) 787-8259

Surface Transportation

Thomas S. Albrecht, CFA (804) 787-8210
 Willard P. Milby, IV (804) 775-7919
 John L. Washington (804) 225-5898
 A. Rhem Wood, Jr. (804) 782-8784

RESEARCH DEPARTMENT

Director of Research

Vernon C. Plack, CFA (804) 780-3257

Assistant Director of Research

James H. Weber, CFA (804) 782-8773

Product Manager

W. Moultrie Dotterer, CFA (804) 780-3279

Supervisory Analysts

Kathleen R. Schneider (732) 567-8766
 Denise Bossé Tyznar (804) 782-8880
 James H. Weber, CFA (804) 782-8773

Editor

Peggy Myers Walz (804) 782-8785

RESEARCH OFFICES

Richmond

Boston

New York

Reston